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Supreme Court, U.S.
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No. 07-

IN THE
Supreme Court of the United States

IMPROV WEST ASSOCIATES and
CALIFORNIA COMEDY, INC.,

Petitioners,

v.

COMEDY CLUB, INC. and
AL COPELAND INVESTMENTS,

Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

PETITION FOR A WRIT OF CERTIORARI

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QUESTIONS PRESENTED

The Ninth Circuit vacated an arbitration award, which was based upon a good faith and reasoned analysis of state law, on the non-statutory ground that the award was in "manifest disregard of the law." Subsequently, in *Hall Street Associates, L.L.C. v. Mattel, Inc.*, 552 U.S. ____, No. 06-989, slip op. 1-15 (March 25, 2008), this Court held that the statutory grounds for vacating, modifying, or correcting an arbitration award specified in the Federal Arbitration Act, 9 U.S.C. §§ 10 and 11, are exclusive and that no non-statutory grounds for vacatur exist. This petition presents the following questions:

1. Whether the Ninth Circuit's decision vacating an arbitration award on the non-statutory ground of "manifest disregard" is inconsistent with this Court's subsequent decision in *Hall Street Associates, L.L.C. v. Mattel, Inc.*, 552 U.S. ___, No. 06-989, slip op. 1-15 (March 25, 2008).

2. Whether an arbitrator's good faith but, in the view of the reviewing court, erroneous interpretation of state law constitutes a basis for vacating an arbitration award under the Federal Arbitration Act, 9 U.S.C. §§ 10 and 11.

CORPORATE DISCLOSURE STATEMENT

The Petitioners, Improv West Associates and California Comedy, Inc., have no parent corporations, and no publicly held company owns 10% or more of their stock.

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PETITION FOR WRIT OF CERTIORARI

Petitioners Improv West Associates and California Comedy, Inc. petition this Court for a Writ of Certiorari to review the judgment of the United States Court of Appeals for the Ninth Circuit entered in this case on September 7, 2007. The Ninth Circuit denied the Petitioners' petition for rehearing and rehearing *en banc* on January 23, 2008.

OPINIONS BELOW

The Arbitrator's Order Re Motions for Summary Adjudication is reprinted at Petitioners' Appendix I. The Arbitrator's Opinion denying the Respondents' motion for reconsideration is reprinted at Petitioners' Appendix H.

The District Court's Order Confirming Arbitration Award, dated April 12, 2005, is reprinted at Petitioners' Appendix C.

The published opinion of the United States Court of Appeals for the Ninth Circuit affirming in part, vacating in part, and remanding to the District Court for further proceedings, dated September 7, 2007, is reprinted at Petitioners' Appendix B.

The published amended opinion of the United States Court of Appeals for the Ninth Circuit affirming in part, vacating in part, and remanding to the District Court for further proceedings, dated January 23, 2008, is reprinted at Petitioners' Appendix A.

JURISDICTION

The United States Court of Appeals for the Ninth Circuit entered judgment on September 7, 2007, and denied the Petitioners' petition for rehearing and rehearing *en banc* on January 23, 2008. This Court has jurisdiction pursuant to 28 U.S.C. § 1254(1).

STATUTORY PROVISIONS INVOLVED

The Federal Arbitration Act, 9 U.S.C. §§ 9-11, provides:

> § 9. Award of arbitrators; confirmation; jurisdiction; procedure
>
> If the parties in their agreement have agreed that a judgment of the court shall be entered upon the award made pursuant to the arbitration, and shall specify the court, then at any time within one year after the award is made any party to the arbitration may apply to the court so specified for an order confirming the award, and thereupon the court must grant such an order unless the award is vacated, modified, or corrected as prescribed in sections 10 and 11 of this title. If no court is specified in the agreement of the parties, then such application may be made to the United States court in and for the district within which such award was made. Notice of the application shall be served upon the adverse party, and thereupon the court shall have jurisdiction of such party as though he had appeared generally in the proceeding. If the adverse

party is a resident of the district within which the award was made, such service shall be made upon the adverse party or his attorney as prescribed by law for service of notice of motion in an action in the same court. If the adverse party shall be a nonresident, then the notice of the application shall be served by the marshal of any district within which the adverse party may be found in like manner as other process of the court.

§ 10. Same; vacation; grounds; rehearing

(a) In any of the following cases the United States court in and for the district wherein the award was made may make an order vacating the award upon the application of any party to the arbitration—

(1) where the award was procured by corruption, fraud, or undue means;

(2) where there was evident partiality or corruption in the arbitrators, or either of them;

(3) where the arbitrators were guilty of misconduct in refusing to postpone the hearing, upon sufficient cause shown, or in refusing to hear evidence pertinent and material to the controversy; or of any other misbehavior by which the rights of any party have been prejudiced; or

(4) where the arbitrators exceeded their powers, or so imperfectly executed them that a mutual, final, and definite

award upon the subject matter submitted was not made.

(b) If an award is vacated and the time within which the agreement required the award to be made has not expired, the court may, in its discretion, direct a rehearing by the arbitrators.

(c) The United States district court for the district wherein an award was made that was issued pursuant to section 580 of title 5 may make an order vacating the award upon the application of a person, other than a party to the arbitration, who is adversely affected or aggrieved by the award, if the use of arbitration or the award is clearly inconsistent with the factors set forth in section 572 of title 5.

§ 11. Same; modification or correction; grounds; order

In either of the following cases the United States court in and for the district wherein the award was made may make an order modifying or correcting the award upon the application of any party to the arbitration—

(a) Where there was an evident material miscalculation of figures or an evident material mistake in the description of any person, thing, or property referred to in the award.

(b) Where the arbitrators have awarded upon a matter not submitted to them, unless it is a matter not affecting the merits of the decision upon the matter submitted.

(c) Where the award is imperfect in matter of form not affecting the merits of the controversy.

The order may modify and correct the award, so as to effect the intent thereof and promote justice between the parties.

STATEMENT OF THE CASE

The District Court in the instant case confirmed an arbitration award that was based on the arbitrator's good faith and reasoned application of state law. The Ninth Circuit held that the arbitrator's reasoning was "fundamentally incorrect" and vacated in part the District Court's order on the non-statutory ground of "manifest disregard of the law." The Ninth Circuit's decision conflicts with this Court's subsequent ruling in *Hall Street Associates, L.L.C. v. Mattel, Inc.*, 552 U.S. ____, No. 06-989, slip op. 1-15 (March 25, 2008), in which this Court held that the statutory grounds for vacating, modifying, or correcting an arbitration award specified in the Federal Arbitration Act ("FAA"), 9 U.S.C. §§ 10 and 11, are exclusive and that no non-statutory grounds for vacatur exist. Furthermore, irrespective of this Court's holding in *Hall Street*, the Ninth Circuit's decision conflicts with the decisions of this Court and of every other circuit in holding that an arbitrator's

good faith but erroneous interpretation of state law is a ground for vacatur under the FAA.

The Petitioners and the Respondents are parties to a Trademark License Agreement dated June 13, 1999 (the "Agreement") pursuant to which the Petitioners granted the Respondents a license to use the Petitioners' "IMPROV" and "IMPROVISATION" trademarks, along with related trade dress and trade secrets, in connection with comedy club franchises across the country through May 13, 2019. The Agreement contains a covenant against competition that restrains the Respondents from operating competing comedy clubs during the term of the Agreement.

A number of disputes arose between the parties that were collectively submitted to mandatory arbitration under the Agreement. One of those disputes was a challenge by Respondents to the enforceability under California Business and Professions Code § 16600 ("CBPC § 16600") of the covenant not to compete. The arbitrator issued two reasoned orders in which he carefully considered CBPC § 16600 and the California and out-of-state cases applying the statute and determined that the Agreement's in-term covenant not to compete was enforceable under those authorities. App. 104a–110a.

The District Court confirmed the arbitration award by an order dated August 29, 2005. App. 77a–78a. The jurisdiction of the District Court was based on 28 U.S.C. § 1332.

On appeal, the United States Court of Appeals for the Ninth Circuit held that "the arbitrator's

ruling that [the covenant] is a valid covenant not to compete ignores CBPC § 16600 and thus is in manifest disregard of the law." App. 27a. The Ninth Circuit acknowledged that the arbitrator had considered and analyzed both CBPC § 16600 and the applicable case law but held that the arbitrator's interpretation of those authorities was "fundamentally incorrect." *Id.* The Ninth Circuit determined that the arbitrator's good faith but, in its view, erroneous application of state law constituted "manifest disregard," which, under Ninth Circuit law, presented a non-statutory basis for vacating the award. App. 29a.[1]

REASONS FOR GRANTING THE PETITION

I. THE NINTH CIRCUIT'S DECISION WAS ISSUED PRIOR TO, AND APPLIES A STANDARD INCONSISTENT WITH, THIS COURT'S DECISION IN *HALL STREET ASSOC., L.L.C. v. MATTEL, INC.*

This petition should be granted and the case remanded because the Ninth Circuit's decision conflicts with this Court's recent decision in *Hall Street Assoc., L.L.C. v. Mattel, Inc.*, 552 U.S. ___, No. 06-989, slip op. 1-15 (March 25, 2008). *See* Rules of the Supreme Court of the United States, Rule 10(c).

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[1] In a separate part of its decision, the Ninth Circuit held that the arbitrator had exceeded the scope of his authority solely by extending an injunction to reach certain non-parties and directed the District Court on remand to modify the injunction to exclude those non-parties. App. 13a-17a. Petitioners do not challenge that part of the Ninth Circuit's decision in this petition.

The instant case was decided before *Hall Street*. As of that time, the Ninth Circuit recognized "a non-statutory escape valve from an arbitral award where the arbitrator has manifestly disregarded the law." *Luong v. Circuit City Stores, Inc.*, 368 F.3d 1109, 1112 (9th Cir. 2004).[2] The Ninth Circuit availed itself of that non-statutory escape valve in this case, holding that the arbitrator's "fundamentally incorrect" understanding of CBPC § 16600 constituted "manifest disregard" requiring vacatur. App. 27a.

In *Hall Street*, this Court held that the statutory grounds for vacating, modifying, or correcting an arbitration award specified in the FAA, 9 U.S.C. §§ 10 and 11, are exclusive and that no non-statutory grounds for vacatur exist. The Ninth Circuit's decision in the present case therefore conflicts with this Court's decision in *Hall Street*, and the decision should be vacated and remanded for reconsideration in light of *Hall Street*.

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[2] Prior to *Luong*, the Ninth Circuit had suggested that section 10(a)(4) of the Federal Arbitration Act might encompass situations where the arbitrator acted "in manifest disregard of the law." *See Kyocera Corp. v. Prudential-Bache Trade Services, Inc.*, 341 F.3d 987, 1002 (9th Cir. 2003); *Todd Shipyards Corp. v. Cunard Line, Ltd.*, 943 F.2d 1056, 1059-60 (9th Cir. 1991). However, in *Luong*, the Ninth Circuit determined that manifest disregard was a "non-statutory escape valve" from sections 10 and 11 of the FAA rather than a statutory ground for vacatur. *Luong*, 368 F.3d at 1112.

II. THE NINTH CIRCUIT'S HOLDING THAT AN ARBITRATOR'S GOOD FAITH BUT ERRONEOUS APPLICATION OF STATE LAW IS A GROUND FOR VACATUR UNDER THE FEDERAL ARBITRATION ACT CONFLICTS WITH THIS COURT'S DECISIONS AND THE LAW OF EVERY OTHER CIRCUIT.

In holding that an arbitrator's good faith but, in the view of the reviewing court, erroneous interpretation of state law constitutes a ground for vacatur, the Ninth Circuit's decision conflicts with the decisions of this Court and of every other circuit applying the FAA and, if permitted to stand, will open the floodgates for plenary review of arbitration awards based on mere errors of law.

The arbitrator in this case considered and rejected the Respondent's challenge to the Agreement's non-compete covenant in a reasoned decision. The arbitrator ruled that the covenant did not unlawfully restrain the Respondents from engaging in an entire trade or profession because it operated only during the term of the Agreement. Pertinent portions of the arbitrator's analysis are quoted below:

> ... Although the language of Section 16600 is broad in scope, court decisions have upheld agreements limiting competition in a variety of contexts. For example, it has been held that Section 16600 applies only to covenants preventing one from engaging in an *entire* business, trade or profession." Campbell

v. Board of Trustees of Stanford University, 817 F.2d 499, 502 (9th Cir. 1987). And covenants not to compete *during the term* of an employment agreement or distribution contract are regularly upheld. Shaklee U.S., Inc. v. Giddens, 1991 U.S. App. LEXIS 11617, *8-9 (9th Cir. 1991).

...

The authorities cited by the parties support the enforceability of in-term covenants not to compete. Such covenants have been held enforceable during the terms of employment[] agreements, Fowler v. Varian Assoc's Inc., 196 Cal. App. 3d 34, 44 (1987), supplier-distributor arrangements, Keating v. Baskin-Robbins, USA, Co., 2001 WL 407017 (E.D.N.C.) (applying California law) and Great Frame-Up Systems, Inc. v. Jazayeri Enterprises, Inc., 789 F. Supp. 253 (E.D. Ill. 1992) (applying California law). Although the reasoning in these decisions is sparse, they do emphasize that in-term restrictions are only "partial" restraints on competition, because the restrained party (whether employee, distributor, or franchisee) may continue to engage in the relevant business during the term of his or her agreement with the employer, supplier or franchisor. Respondent has not cited any decision invalidating in-term covenants not to compete under Section 16600. The arbitrator finds, therefore,

> that paragraph 9.j of the Agreement is a valid and enforceable in-term covenant under California law.

App. 105a, 108a.

In confirming the arbitration award, the District Court acknowledged that the arbitrator had "spent several pages explaining its position with regards to the non-compete clause" and also that the arbitrator's ruling "finds support in the case law," including both California and out-of-state cases applying CBPC § 16600. App. 72a-73a. The Ninth Circuit nonetheless vacated in part the District Court's order confirming the award, holding that the arbitrator's ruling "ignore[d]" CBPC § 16600 and was therefore "in manifest disregard of the law." App 27a.

The Ninth Circuit's holding that an arbitrator's good faith but, in its view, erroneous application of state law requires vacatur of an arbitration award conflicts with this Court's decisions and the law of every circuit. As this Court explained in *Hall Street*, sections 10 and 11 of the FAA address "egregious departures from the parties' agreed-upon arbitration" such as "corruption," "fraud," "evident partiality," "misconduct," and "misbehavior." *Hall Street*, 552 U.S. at __, slip op. at 9. This Court has contrasted these "specific instances of outrageous conduct" with "review for just any legal error," observing that "[f]raud and a mistake of law are not cut from the same cloth." *Id.*, slip op. at 9-10.

Every Court of Appeals has carefully distinguished between a good faith error of law, which is never a basis for vacating an arbitration award, and deliberate defiance of the law. As the Eight Circuit explained in *Lincoln Nat'l Life Ins. Co. v. Payne*, 374 F.3d 672, 674 (8th Cir. 2004):

> Manifest disregard requires something more than a mere error of law. If an arbitrator, for example, stated the law, acknowledged that he was rendering a decision contrary to law, and said that he was doing so because he thought the law unfair, that would be an instance of 'manifest disregard.' ... To require anything less would threaten to subvert the arbitral process.

Advest, Inc. v. McCarthy, 914 F.2d 6, 10 (**1st Cir.** 1990) ("'[D]isregard' implies that the arbitrators appreciated the existence of a governing legal rule but willfully decided not to apply it."); *Wallace v. Buttar*, 378 F.3d 182, 190 (**2d Cir.** 2004) ("A federal court cannot vacate an arbitral award merely because it is convinced that the arbitration panel made the wrong call on the law."); *Local 863 Int'l Bhd. of Teamsters v. Jersey Coast Egg Producers, Inc.*, 773 F.2d 530, 533 (**3d Cir.** 1985) ("An award may be set aside only in limited circumstances, for example, where the arbitrator's decision evidences manifest disregard for the law rather than an erroneous interpretation of the law."); *Remmy v. PaineWebber, Inc.*, 32 F.3d 143, 149 (**4th Cir.** 1994) ("[A] court's belief that an arbitrator misapplied the law will not justify vacation of an arbitral award.

Rather, appellant is required to show that the arbitrators were aware of the law, understood it correctly, found it applicable to the case before them, and yet chose to ignore it in propounding their decision."); *Brabham v. A.G. Edwards & Sons Inc.*, 376 F.3d 377, 381 (**5th Cir.** 2004) ("Manifest disregard means more than error or misunderstanding with respect to the law.") (internal quotation marks omitted); *Merrill Lynch, Pierce, Fenner & Smith v. Jaros*, 70 F.3d 418, 421 (**6th Cir.** 1995) ("This court has emphasized that manifest disregard of the law is a very narrow standard of review. A mere error in interpretation or application of the law is insufficient.") (internal citation omitted); *Butler Mfg. Co. v. United Steelworkers of Am.*, 336 F.3d 629, 636 (**7th Cir.** 2003) ("[A]n arbitral decision is in manifest disregard of the law only when the arbitrator's award actually orders the parties to violate the law. That the arbitrator in this case may have misunderstood the [governing statute] is simply not relevant.") (internal citation omitted); *Stroh Container Co. v. Delphi Indus., Inc.*, 783 F.2d 743, 750 (**8th Cir.** 1986) (manifest disregard "may be found when arbitrators understand and correctly state the law, but proceed to disregard the same"); *Bowen v. Amoco Pipeline Co.*, 254 F.3d 925, 932 (**10th Cir.** 2001) ("Requiring more than error or misunderstanding of the law, a finding of manifest disregard means the record will show the arbitrators knew the law and explicitly disregarded it.") (internal citation omitted); *Aldred v. Avis Rent-A-Car*, No. 06-14883, 2007 WL 2110720, at *2 (**11th Cir.** July 24, 2007) ("An arbitrator manifestly disregards the law if he was conscious of the law and

deliberately ignored it; merely misinterpreting, misstating, or misapplying the law does not suffice."); *Kanuth v. Prescott, Ball & Turben, Inc.*, 949 F.2d 1175, 1182 (D.C. Cir. 1991) ("'Manifest disregard' may be found, for example, if the panel understood and correctly stated the law but then proceeded to ignore it."). Thus, the focus in every circuit is not on whether the arbitrator got the law right or wrong, but instead on whether he or she made a good faith effort to correctly apply the law.

The Ninth Circuit's decision in this case dramatically alters this "manifest disregard" standard for review of an arbitration award. Whether or not the arbitrator misinterpreted CBPC § 16600 and the cases arising thereunder, it is abundantly clear that he neither ignored nor acted in deliberate defiance of California law. The arbitrator's written orders devoted several pages to a discussion of CBPC § 16600 and its application to the facts of this case. The Ninth Circuit's belief that the arbitrator was wrong is not a ground for vacatur under sections 10 and 11 of the FAA.

CONCLUSION

The Ninth Circuit's decision vacating in part an arbitration award based on the non-statutory ground of "manifest disregard" is inconsistent with this Court's subsequent decision in *Hall Street*. Furthermore, the Ninth Circuit's holding that an arbitrator's good faith but erroneous application of state law is a basis for vacatur under the Federal Arbitration Act conflicts with the uniform precedent of every other circuit.

This Court should grant certiorari, vacate the decision of the Ninth Circuit, and remand this case for further consideration in light of *Hall Street*.

Respectfully submitted,

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Appendix A

United States Court of Appeals, Ninth Circuit

NOS. 05-55739, 05-56100

COMEDY CLUB, INC., a Louisiana corporation; Al Copeland Investments, Inc., a Louisiana corporation,

Plaintiffs-Appellants,

v.

IMPROV WEST ASSOCIATES, a California Limited Partnership; California Comedy, Inc., a California corporation,

Defendants-Appellees.

Comedy Club, Inc., a Louisiana corporation; Al Copeland Investments, Inc., a Louisiana corporation,

Plaintiffs-Appellants,

v.

Improv West Associates, a California Limited Partnership; California Comedy, Inc., a California corporation,

Defendants-Appellees.

Jan. 23, 2008

AMENDED OPINION

Before: JEROME FARRIS and RONALD M. GOULD, Circuit Judges, and KEVIN THOMAS DUFFY,* District Judge.

GOULD, Circuit Judge:

On June 13, 1999, Comedy Club, Inc. and Al Copeland Investments, Inc. (collectively "CCI") executed a Trademark License Agreement ("Trademark Agreement") with Improv West Associates ("Improv West") that granted CCI an exclusive nationwide license to use Improv West's trademarks. A few years later, CCI breached the agreement and sought to protect its interests in the trademarks in federal district court by filing a declaratory judgment action. After a complex procedural history, the parties were left with an arbitration award and two district court orders, one order compelling the parties to arbitrate, and another order confirming the arbitration award. CCI appeals both district court orders. We have jurisdiction under 28 U.S.C. §1291. We lack jurisdiction to review the district court's order compelling arbitration. We affirm in part and vacate in part the district court's order confirming the arbitration award, and we remand to the district court for further proceedings.

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* The Honorable Kevin Thomas Duffy, Senior United States District Judge for the Southern District of New York, sitting by designation.

I

Improv West is the founder of the Improv Comedy Club and the creator and owner of the "Improv" and "Improvisation" trademarks ("Improv marks"). CCI owns and operates restaurants and comedy clubs nationwide. On June 13, 1999, CCI and Improv West entered a Trademark Agreement[1] that provided, *inter alia*: (1) that Improv West granted CCI an exclusive nationwide license to use the Improv marks in connection with the opening of new comedy clubs; (2) that, according to a development schedule, CCI was to open four Improv clubs a year in 2001 through 2003;[2] and (3) that CCI was prohibited from opening any non-Improv comedy clubs during the term of the Trademark Agreement.[3] The Trademark Agreement also had an arbitration clause:

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[1] Also on June 13, 1999, in a separate Asset Purchase Agreement, CCI purchased the Melrose Improv Club from Improv West. The Melrose Improv Club is located in Los Angeles, California.

[2] The original §12.a. of the Trademark Agreement called for CCI to open and operate at least three Improv clubs by 2001, and two each year thereafter so that CCI would own and operate at least seven Improv clubs by 2003. CCI and Improv West amended §12.a. on October 19, 1999, creating the schedule of four Improv clubs a year in 2001 through 2003.

[3] Section 9j. of the Trademark Agreement stated: "Licensee shall not own or operate, and Licensee shall ensure that none of its Affiliates shall own or operate any bar, restaurant, nightclub, or other facility which presents live stand-up or sketch comedy performances or live improvisational performances, other than the Melrose Improv or a Club, or Second City."

> All disputes relating to or arising under this Agreement or the Asset Purchase Agreement shall be resolved by arbitration in Los Angeles, California in accordance with the commercial arbitration rules of the American Arbitration Association. In any such arbitration, the parties shall be entitled to discovery in the same manner as if the dispute was being litigated in Los Angeles Superior Court. Notwithstanding this agreement to arbitrate, the parties, in addition to arbitration, shall be entitled to pursue equitable remedies and agree that the state and federal courts shall have exclusive jurisdiction for such purpose and for the purpose of compelling arbitration and/or enforcing any arbitration award. The parties agree to submit to the jurisdiction of such courts and agree that service of process in any such action may be made by certified mail. The prevailing party in any arbitration or action to enforce this Agreement or the Asset Purchase Agreement shall be entitled to its costs, including reasonable attorneys fees.

CCI concedes that it failed to open eight Improv clubs by 2002,[4] and that it was in default of amended §12.a. of the Trademark Agreement. Consistent with Improv West's sole remedy, as

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[4] In CCI's original complaint, CCI claims that it opened or obtained an interest in at least seven Improv clubs, not including the Melrose Improv Club.

stated in §13.b.,[5] Improv West sent CCI a letter asserting that CCI was in default of the Trademark Agreement, withdrawing CCI's license to use the Improv marks and rights to open more Improv clubs, and informing CCI that Improv West intended to begin opening its own Improv clubs.

In response to Improv West's letter, CCI filed a complaint in federal district court seeking declaratory relief. CCI's complaint sought a declaration that the covenant that CCI could not open any non-Improv comedy clubs was void under California Business and Professions Code ("CBPC") §16600, and that CCI's failure to meet the development schedule did not revoke CCI's license to the Improv marks or right to open Improv clubs. Improv West then filed a demand for arbitration seeking damages.[6]

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[5] Section 13.b. of the Trademark Agreement provided Improv West's sole remedy in the event CCI defaulted on the §12.a. development schedule. In pertinent part, §13.b. stated:

> Notwithstanding the above enumerated remedies, in the event [CCI] fails to fulfill the schedule set forth in section 12.a., [Improv West's] sole remedy shall be as follows. Upon notice to [CCI], [CCI] shall lose the right, power, and License (i) to use the Trademarks in connection with any Clubs which are not, as of the date of such failure, under construction or open for business and operated by [CCI], an Affiliate of [CCI] or other Operator and (ii) to sub-license Third Parties use of the Trademarks in connection with any new Clubs.

[6] In a further response, CCI amended its complaint seeking to enjoin Improv West from opening, or authorizing third parties to open, any Improv clubs, and asking for disgorgement

On August 2, 2004, the district court ordered the parties to arbitrate their dispute. CCI did not appeal that order until May 16, 2005.

On February 28, 2005, the arbitrator entered a Partial Final Arbitration Award that stated: (1) that CCI defaulted on the Trademark Agreement by failing to adhere to the development schedule listed in amended §12.a.; (2) that CCI forfeited its rights to open Improv clubs and its use of the Improv marks license in connection with any clubs not open or under construction as of October 15, 2002; (3) that Improv West could open or license to third parties new Improv clubs; (4) that §9j of the Trademark Agreement was "a valid and enforceable in-term covenant not to compete" and remained valid "for the remaining term of the Agreement"7; (5) that CCI and its "Affiliates"8 were enjoined from opening or operating any other comedy clubs other than those

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of Improv West's profits from any such action.

[7] Unless the parties agree to terminate the Trademark Agreement earlier, by its own terms, the Trademark Agreement does not end until 2019.

[8] Section 1 of the Trademark Agreement stated, in relevant part, that "'a Person' is "any natural person, or any corporation, partnership, joint venture, limited liability company, business association, trust ... or other entity," and that the term "Affiliate" means and includes "any members of such Person's immediate family, or the member of the immediate family of any direct or indirect shareholder of such Person.... Further, the members of the immediate family of any Person shall include all collateral relatives of such Person having a common linear ancestor with such Person, and the spouse or any former spouse of such Person or any of such collateral relatives of such spouse."

open or under construction as of October 15, 2002 for the duration of the Trademark Agreement; (6) that neither CCI nor its Affiliates could change the name on any of its current clubs; and (7) that Improv West was entitled to attorneys fees and costs. On April 14, 2005, the district court confirmed the Partial Award. CCI timely appealed, tendering to us the issues addressed in this opinion.[9]

II

CCI first argues that the district court erred when it issued its order compelling the parties to arbitrate. Improv West in turn contends that we lack jurisdiction over this issue because CCI's appeal of the district court's order compelling arbitration is untimely.

The district court's order compelling the parties to arbitrate dismissed CCI's claims when it sent the parties to arbitration. Because the district court's order dismissed CCI's claims, it is a final order. *See Green Tree Fin. Corp. v. Randolph*, 531 U.S. 79, 86, 121 S.Ct. 513, 148 L.Ed.2d 373 (2000) (holding that a district court's order dismissing the

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[9] Although all the issues in this appeal concern the arbitrator's decision in the Partial Final Arbitration Award entered on February 28, 2005, the arbitrator issued a second arbitral award, the Final Arbitration Award, which was decided on May 20, 2005. The district court confirmed that award on June 21, 2005, and entered judgment on August 29, 2005. CCI timely appealed the district court's order confirming the Final Arbitration Award on July 20, 2005, but raised no issues on appeal concerning that award. We consolidated the two cases for appeal purposes.

plaintiffs claims and compelling arbitration was a final decision because the order "end[ed] the litigation on the merits and le[ft] nothing more for the court to do but execute the judgment" (internal quotation marks omitted)); *see also* 9 U.S.C. §16(a)(3) (2006) ("An appeal may be taken from ... a final decision with respect to an arbitration that is subject to this title."); 9 U.S.C. §16(a)(3) prac. cmt. (instructing that subdivision (a)(3) makes appealable a district court's determination compelling arbitration that is a final decision); *Bushley v. Credit Suisse First Boston,* 360 F.3d 1149, 1153 n.1 (9th Cir. 2004) (adopting the principle that "a dismissal renders an order appealable under §16(a)(3)" (citation omitted)).

28 U.S.C. §2107(a) and Federal Rule of Appellate Procedure 4(a)(1) require that a notice of appeal be filed in a civil case "within 30 days after the judgment or order appealed from is entered." Fed. R. App. P. 4(a)(1)(A). Because the district court did not enter judgment on the order to compel arbitration, CCI had 180 days to appeal the order. *See* Fed. R.App. P. 4(a)(7)(A)(ii); *see also Bowles v. Russell,* --- U.S. ----, 127 S.Ct. 2360, 2363, 168 L.Ed.2d 96 (2007) (stating that "the taking of an appeal within the prescribed time is mandatory and jurisdictional" (internal quotation marks omitted)).

CCI filed its first notice of appeal of the district court's order compelling arbitration on May 16, 2005, 287 days after the order was entered on August 2, 2004. This is well beyond the 180 days allowed by Federal Rule of Appellate Procedure 4(a)(7)(A)(ii). CCI's appeal of the district court's

order compelling arbitration is untimely, and we lack jurisdiction to hear the appeal of that issue.

III

We next consider CCI's contention that the district court erred by confirming the arbitration award. We review a district court's confirmation of an arbitration award de novo. *See First Options of Chi., Inc. v. Kaplan,* 514 U.S. 938, 947-48, 115 S.Ct. 1920, 131 L.Ed.2d 985 (1995). CCI presents four arguments: (1) that the arbitrator lacked authority to arbitrate the equitable claims; (2) that the arbitrator exceeded the scope of his authority by issuing two permanent injunctions; (3) that the arbitrator's award is irrational; and (4) that the arbitrator's award violates CBPC §16600. We address each argument in turn.

A

CCI submits that the arbitrator lacked authority to arbitrate because the arbitration clause in the Trademark Agreement grants state and federal courts an "exclusive" jurisdiction over equitable claims. We review the validity and scope of an arbitration clause de novo. *See Moore v. Local 569 of Int'l Bhd. of Elec. Workers,* 53 F.3d 1054, 1055-56 (9th Cir. 1995).

It is well established "that where the contract contains an arbitration clause, there is a presumption of arbitrability." *AT & T Techs., Inc. v. Commc'ns Workers of Am.,* 475 U.S. 643, 650, 106 S.Ct. 1415, 89 L.Ed.2d 648 (1986). "[A]n order to arbitrate the particular grievance should not be

denied unless it may be said with positive assurance that the arbitration clause is not susceptible of an interpretation that covers the asserted dispute. Doubts should be resolved in favor of coverage." *Id.*; *see also Three Valleys Mun. Water Dist. v. E.F. Hutton & Co.*, 925 F.2d 1136, 1139 (9th Cir. 1991) ("Under the Federal Arbitration Act ... any doubts concerning the scope of arbitrable issues should be resolved in favor of arbitration...." (internal quotation marks and citation omitted)).

It is also well established that "[w]hen deciding whether the parties agreed to arbitrate a certain matter ... courts generally ... should apply ordinary state-law principles that govern the formation of contracts." *First Options*, 514 U.S. at 944, 115 S.Ct. 1920. Only disputes "that the parties have agreed to submit to arbitration" should be arbitrated. *Id.* at 943, 115 S.Ct. 1920; *see also Republic of Nicar. v. Standard Fruit Co.*, 937 F.2d 469, 478 (9th Cir. 1991) (stating that "[t]he scope of the [arbitration] clause must ... be interpreted liberally").

Under California contract law, "if the language [of a contract] is clear and explicit, and does not involve an absurdity" the language must govern the contract's interpretation. Cal. Civ.Code §1638. Moreover, when a contract is written, "the intention of the parties is to be ascertained from the writing alone, if possible." Cal. Civ.Code §1639. "[I]f reasonably practicable" a contract must be interpreted as a whole, "so as to give effect to every part, ... each clause helping to interpret the other." Cal. Civ.Code §1641; *see also In re Affordable Hous.*

Dev. Corp., 175 B.R. 324, 329 (9th Cir. BAP 1994) ("California law provides that one phrase of a contract should not be interpreted so as to render another phrase of the contract meaningless."). However, "[i]f a contract is capable of two different reasonable interpretations, the contract is ambiguous," *Oceanside 84, Ltd. v. FId. Fed. Bank,* 56 Cal.App.4th 1441, 1448, 66 Cal.Rptr.2d 487 (1997), and under the federal presumption in favor of arbitration, an arbitrator would have jurisdiction to arbitrate claims. *See AT & T Techs.*, 475 U.S. at 650, 106 S.Ct. 1415; Three Valleys, 925 F.2d at 1139.

Applying these principles, we conclude that the Trademark Agreement's arbitration clause grants the arbitrator authority over "all disputes" arising from the Trademark Agreement. There are three relevant clauses in the arbitration agreement: (1) "[a]ll disputes relating to or arising under this Agreement ... shall be resolved by arbitration"; (2) "[n]otwithstanding this agreement to arbitrate, the parties, in addition to arbitration, shall be entitled to pursue equitable remedies and agree that the state and federal courts shall have exclusive jurisdiction for such purpose and for the purpose of compelling arbitration and/or enforcing any arbitration award"; and (3) "[t]he prevailing party in any arbitration or action to enforce this Agreement ... shall be entitled to its costs, including reasonable attorneys fees."

CCI contends that clause two is explicit that only state and federal courts, and not an arbitrator, have jurisdiction over equitable claims. Improv West counters that the second clause only carved out

equitable claims "in aid of arbitration" to maintain the status quo between the parties pending arbitration, and that the second clause did not "supplant the arbitrator's authority" to decide all disputes under the Trademark Agreement.

A natural reading of clause two lends plausibility to Improv West's theory. The language "in addition to arbitration" in clause two suggests that arbitration still applies to all disputes, but that in addition, the parties are "entitled to pursue equitable remedies" before courts. If the parties intended to carve out an exception to arbitration for all equitable claims, they could have done so without the language "in addition to arbitration." Because the parties included this language, it is plausible and a permissible contract interpretation that the equitable claims exception in clause two was intended to apply only to claims designed to maintain the status quo between the parties. Stated another way, it was a rational interpretation of the agreement to say that the arbitrator could decide both equitable and legal claims and that the provision for court jurisdiction on equitable matters was ancillary to the arbitration. Moreover, the Federal Arbitration Act, 9 U.S.C. §3, provides a court with the ability to stay "trial of [an] action until such arbitration has been had," but it does not give a court the authority to issue equitable remedies, such as a temporary injunction, to maintain the status quo between the parties. Thus, it makes sense that if the parties wanted to give themselves the a on coverage over "all disputes" arising from the Trademark Agreement. *See AT&T Techs.*, 475 U.S. at 650, 106 S.Ct. 1415; *Three Valleys*, 925 F.2d at

1139. We hold that the arbitration agreement gave the arbitrator authority over all disputes, equitable and legal, and that he did not exceed his authority by arbitrating equitable claims.

B

We next address CCI's argument that the arbitrator exceeded the scope of his authority in issuing two permanent injunctions, which would provide grounds to vacate the arbitration award. *See Coutee v. Barington Capital Group, L.P.*, 336 F.3d 1128, 1134 (9th Cir. 2003); 9 U.S.C. §10(a)(4).

In his partial arbitration award, the arbitrator (1) enjoined CCI and its Affiliates from opening or operating any other comedy clubs other than those open or under construction as of October 15, 2002 for the duration of the Trademark Agreement and (2) enjoined CCI and its Affiliates from changing the name on any of their current clubs until the Trademark Agreement ended. CCI argues that because the Trademark Agreement defines Affiliates to include "family members, family members of shareholders, all collateral relatives,[10] former spouses, and all collateral relatives of former spouses," the permanent injunctions attempt to bind persons beyond the scope of the arbitrator's authority.[11] We agree.

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[10] Black's Law Dictionary defines "collateral relative" as "[a] relative who is not in the direct line of descent, such as a cousin." Black's Law Dictionary 1315 (8th ed. 2004).

[11] CCI raises this issue for the first time on appeal. Although we generally do "not consider an issue raised for the

A contract may bind non-parties such as an intended third party beneficiary, an agent, or an assignee. *See Benasra v. Marciano,* 92 Cal.App.4th 987, 991, 112 Cal.Rptr.2d 358 (2001). But generally arbitration clauses and contracts do not bind non-parties in the absence of such extraordinary relationships. As explained in *Buckner v. Tamarin,* 98 Cal.App.4th 140, 119 Cal.Rptr.2d 489 (2002): "The strong public policy in favor of arbitration does not extend to those who are not parties to an arbitration agreement...." *Id.* at 142, 119 Cal.Rptr.2d 489 (internal quotation marks omitted); *see also NORCAL Mut. Ins. Co. v. Newton,* 84 Cal.App.4th 64, 76, 100 Cal.Rptr.2d 683 (2000) ("The common thread... is the existence of an agency or similar relationship between the nonsignatory and one of the parties to the arbitration agreement. In the absence of such a relationship, courts have refused to hold nonsignatories to arbitration agreements.").

Here, the arbitrator's injunctions, relying on the Trademark Agreement's definition of Affiliate, seek to prevent people such as cousins of former

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first time on appeal," we recognize three exceptions to that rule, by which we may invoke our discretion and review the issue: (1) where "review is necessary to prevent a miscarriage of justice or to preserve the integrity of the judicial process"; (2) where there is a change in the law creating a new issue; or (3) "when the issue presented is purely one of law and either does not depend on the factual record developed below, or the pertinent record has been fully developed." *Cold Mountain v. Garber,* 375 F.3d 884, 891 (9th Cir. 2004) (internal quotation marks and citation omitted). Here, we exercise our discretion and review CCI's argument under exceptions one and three.

spouses of CCI partners from opening or operating any comedy club within the United States until 2019. These collateral relatives are not in privity with the Trademark Agreement signatories, or with CCI shareholders, partners, or "persons." As an example, it is not reasonable to preclude from gainful competition in the comedy club sphere relatives of ex-spouses of the CCI principals who were not in an agency relationship with those principals. Similarly, the arbitrator did not have authority to enjoin a non-party grandmother of a CCI partner from opening a restaurant with live stand up comedy performance until the year 2019. Under California law, the arbitrator lacked the authority to enjoin these non-parties from owning or operating comedy related businesses or restaurants.

Improv West contends that Federal Rule of Civil Procedure 65(d) ("Rule 65(d)") establishes that an injunction may bind not only parties to the action but also "their officers, agents, servants, employees, and attorneys, and [upon] those persons in active concert or participation with them." Fed.R.Civ.P. 65(d). However, the wholesale inclusion of relatives as Affiliates in the Trademark Agreement's covenant not to compete, and the injunctions in the arbitrator's partial award, go well beyond binding CCI's agents, employees, or people in active concert or participation with it as Rule 65(d) permits. Indeed, as mentioned above, §9j, by its own terms, reaches beyond persons with an agency or assignee relationship with CCI partners, and literally purports to bind a CCI "person's" ex-wife and his ex-wife's cousins, nephews, uncles, and aunts. The text of Rule 65(d) is exclusive, stating that an injunction

can permissibly bind "only" those persons listed in Rule 65(d). Rule 65(d) does not list collateral relatives of former spouses, or even grandparents, as potential non-parties who may be bound by a contract or an arbitration award. And we do not think it is a proper use of equitable power to restrain all such persons.

Moreover, precluding non-party relatives or ex-spouses from opening or operating improv-comedy-related businesses or restaurants violates CBPC §16600. CBPC §16600 provides, in relevant part, that "every contract by which anyone is restrained from engaging in a lawful profession, trade, or business of any kind is to that extent void." *Id.* This is a codification of "the general rule in California [that] covenants not to compete are void." *Hill Med. Corp. v. Wycoff,* 86 Cal.App.4th 895, 901, 103 Cal.Rptr.2d 779 (2001). By restricting non-party relatives and ex-spouses from engaging in a lawful business, the injunctions, with respect to those persons, exceed the arbitrator's authority.

We conclude that the arbitrator acted beyond the scope of his authority as a matter of California law in attempting to bind all of CCI's Affiliates, including relatives who were not parties to the Trademark Agreement, and thus could not be bound by its provisions. If an arbitrator exceeded the scope of his authority in issuing an award, and that award is divisible, we may vacate part of the award and leave the remainder in force. *See Lyle v. Rodgers,* 18 U.S. (5 Wheat.) 394, 409, 5 L.Ed. 117 (1820) (Marshall, C.J.) (stating that "an award may be void in part, and good for the residue"); *Barington*

Capital, 336 F.3d at 1134("A federal court may vacate an arbitration award, or a portion thereof, if the arbitrators acted beyond their authority."). We therefore conclude that the district court should vacate the arbitration award insofar as it enjoins any of CCI's Affiliates who are not connected to the principals of CCI as, by analogy to Rule 65(d), "their officers, agents, servants, employees, and attorneys, and [upon] those persons in active concert or participation with them." We hold that a narrowing of the restrictive covenant on Affiliates is required by CBPC §16600 and the principle that non-parties generally are not bound in arbitration. Such non-parties can only be restrained to the extent permitted by Rule 65(d).

C

CCI next contends that the partial arbitration award is irrational because it simultaneously revokes CCI's license to open Improv clubs and prevents CCI from opening or operating any other comedy clubs anywhere in the United States until 2019 or the termination of the Trademark Agreement.

Review of an arbitration award is "'both limited and highly deferential'" and the arbitration award "may be vacated only if it is 'completely irrational' or 'constitutes manifest disregard of the law.'" *Poweragent Inc. v. Elec. Data Sys. Corp.,* 358 F.3d 1187, 1193 (9th Cir. 2004) (*quoting Barington Capital,* 336 F.3d at 1132-33). We have not elaborated on what "completely irrational" means, but the Eighth Circuit has persuasively indicated

that the "completely irrational" standard is extremely narrow and is satisfied only "where [the arbitration decision fails to draw its essence from the agreement]." *Hoffman v. Cargill Inc.*, 236 F.3d 458, 461-62 (8th Cir. 2001). This is a view that we adopt.

Under the partial arbitration award, CCI lost its exclusive right to open and operate any new Improv clubs using Improv West's license. And because the arbitrator found the §9j covenant not to compete of the Trademark Agreement valid, CCI also lost the right to open and operate any other new comedy clubs or restaurants under any other license or name anywhere in the contiguous United States as long as the Trademark Agreement remained in effect. Thus, apart from allowing CCI to continue to operate the handful of Improv clubs that it had already opened or purchased, *see supra* note 4, the arbitrator's ruling put CCI out of the comedy club business.

CCI argues that if it has lost all licensing rights, then there is no longer any licensing agreement. Both parties agree that if the Trademark Agreement is no longer in effect then the §9j covenant not to compete similarly would no longer be in effect, and the arbitrator's award would be considered irrational.

However, as Improv West correctly asserts, Improv West did not cancel the Trademark Agreement, neither party sought to terminate the Trademark Agreement as part of the underlying actions, and nothing in the parties' submissions, the arbitrator's rulings, or the district court's orders

suggest that the Trademark Agreement was cancelled. Instead, CCI was still bound under other sections of the Trademark Agreement to pay Improv West royalties on the seven Improv clubs it still operated at the conclusion of the arbitration.

A breach by a party to a contract does not in itself cancel the contract.[12]Cancellation of a contract occurs when "either party puts an end to the contract for breach by the other."[13] *See* Bernard E. Witkin, *Summary of California Law* §925 (10th ed. 2005) (internal quotation marks omitted); *see also* Restatement (Second) of Contracts §274 (1979); 13 Arthur Linton Corbin, *Corbin on Contracts* §67.2 (Rev. ed. 2003).

At the time of arbitration, Improv West had not cancelled, nor had the parties terminated, the contract. In the arbitration Improv West did not seek to terminate the contract. By the arbitrator's own award, the arbitrator did not modify the party's contractual relationship, including the required payment of royalties, on the seven Improv clubs that CCI had opened or bought and was running.

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[12] The general rule is that if the breach is a material breach, it may give grounds for the non-breaching party to cancel the contract, *see Rano v. Sipa Press, Inc.*, 987 F.2d 580, 586 (9th Cir. 1993), but if the breach is a partial breach, the non-breaching party's remedy is for damages. *See Postal Instant Press, Inc. v. Sealy*, 43 Cal.App.4th 1704, 1708-09, 51 Cal.Rptr.2d 365 (1996).

[13] "'Termination occurs when either party pursuant to a power created by agreement or law puts an end to the contract otherwise than for its breach.'" *See* Witkin, *Summary of California Law* §925(internal quotation marks omitted).

Further, per the arbitrator's award, the covenant not to compete ends when the Trademark Agreement ends. CCI will then be able to open up other non-Improv clubs.

CCI entered into the Trademark Agreement with knowledge that there would be consequences if it defaulted on the development schedule in §12.a. of the Trademark Agreement. An arbitrator could rationally decide that the §9j covenant not to compete was valid to some degree, while at the same time upholding Improv West's remedy to end CCI's exclusive license rights to open other Improv clubs.

The basic outline of what the arbitrator did, terminating an exclusive right to open Improv clubs nationwide, because of contractually inadequate performance contrary to the agreed schedule, while keeping in force the restrictive covenant makes sense in so far as CCI should not have an exclusive license on Improv clubs absent complying with designated performance. And so long as CCI was running some Improv clubs, a restrictive covenant to some degree could protect Improv West from damage caused by improper competition. Because we cannot say that there is no basis in the record for the arbitrator's decision, we hold that the arbitrator's award is not completely irrational. *See NF & M*, 524 F.2d at 760.

D

Finally, we address CCI's claim that the partial arbitration award should be vacated because it is in violation of CBPC §16600. CCI argues that

the arbitrator's validation of §9j is in manifest disregard of the law. We have stated that for an arbitrator's award to be in manifest disregard of the law, "[i]t must be clear from the record that the arbitrator [ ] recognized the applicable law and then ignored it." *Mich. Mut. Ins. Co. v. Unigard Sec. Ins. Co.*, 44 F.3d 826, 832 (9th Cir. 1995).

Under CBPC §16600, it is well established that broad covenants not to compete are void unless they involve a situation where "a person sells the goodwill of a business [or] where a partner agrees not to compete in anticipation of dissolution of a partnership," *see Kelton v. Stravinski,* 138 Cal. App. 4th 941, 946, 41 Cal.Rptr.3d 877 (2006), CBPC §§16601, 16602, or "they are necessary to protect trade secrets." *Alliance Payment Sys. v. Walczer,* 152 Cal.App.4th 620, 61 Cal.Rptr.3d 789 (2007). Neither party alleges any of the above exceptions apply in this case.

The majority of cases interpreting CBPC §16600 under California law deal with post-contract or post-employment covenants not to compete. *See, e.g., Alliance Payment Sys.,* 152 Cal.App.4th 620, 61 Cal.Rptr.3d 789, 796; *Thompson v. Impaxx, Inc.,* 113 Cal.App.4th 1425, 1427-29, 7 Cal.Rptr.3d 427 (2003). In this case, the Trademark Agreement has not been terminated or canceled; rather the contractual relationship between CCI and Improv West is ongoing and §9j can be viewed as an in-term covenant not to compete.[14]

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[14] Because Improv West revoked CCI's rights to the Improv marks for almost the entire contiguous United States, the

We have not found, and the parties do not cite, any Ninth Circuit or California cases holding that in-term covenants not to compete of any scope are necessarily valid. There are, however, cases addressing in-term covenants not to compete, and we discuss several of those cases here because of the limitations that we believe they impose under §16600, even in the context of a continuing covenant not to compete.

Most significant to our analysis is *Dayton Time Lock Service, Inc. v. Silent Watchman Corp.*, 52 Cal.App.3d 1, 124 Cal.Rptr. 678 (1975), in which the California Court of Appeal, addressed an in-term "exclusive dealing clause" in a franchise agreement. *Id.* at 6, 124 Cal.Rptr. 678. The exclusive dealing clause provided in part that "during the life of this contract,... [Dayton Time Lock Service, Inc. ("DTLS")] will not sell or lease any locks, devices or service of any kind in competition with the business of[Silent Watchman Corp. ("SW")], or use any time recording lock not supplied by [SW] under this agreement." *Id.* DTLS argued that this anti-

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Improv West-CCI licensing relationship has ended except as to the existing Improv clubs. Bearing this in mind, it might be possible to view §9j, with respect to the majority of the United States, functionally as if it were a post-term covenant not to compete, and with respect to the Improv clubs that CCI continues to operate, as an in-term covenant not to compete. However, because the contract relationship has not been canceled, and continues for the existing Improv clubs operated by CCI, we think it more appropriate conceptually to analyze §9j nationwide as an in-term covenant not to compete, while considering CCI's limited continuing use of the Improv marks as pertinent to the scope of §9j.

competitive provision, along with a separate post-franchise covenant not to compete, violated state and federal antitrust laws. *Id.* The California Court of Appeal first noted that SW conceded that the post-term covenant not to compete violated the state antitrust law CBPC §16600. *Id.* Next, the court specifically addressed whether the in-term covenant not to compete was valid. In this context, the court held that "[e]xclusive-dealing contracts are not necessarily invalid," but "[t]hey are proscribed when it is probable that performance of the contract will foreclose competition in a substantial share of the affected line of commerce." *Id.* In doing so, *Dayton Time Lock* imposed the standards analogous unto federal antitrust law when interpreting §16600. *See id.* (citing *Standard Oil Co. v. United States*, 337 U.S. 293, 314, 69 S.Ct. 1051, 93 L.Ed. 1371 (1949)).[15]

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[15] Similar to *Dayton Time Lock*, the District Court for the Northern District of Illinois in *Great Frame Up Systems, Inc. v. Jazayeri Enterprises*, 789 F.Supp. 253 (N.D.Ill. 1992), stated, while interpreting California law on CBPC §16600, that California courts support the position "that preventing defendants from competing only during the term of [an] existing franchise agreement, would not be void." *Id.* at 255. The court reasoned, however, that the in-term contractual provisions still cannot prevent a party from engaging in an entire profession, business or trade. *See id.* at 256.

Finally, in *General Commercial Packaging, Inc. v. TPS Package Engineering, Inc.*, 126 F.3d 1131 (9th Cir. 1997) (per curiam), we addressed a covenant not to compete in a general contractor-subcontractor context. General Commercial Packaging ("GCP"), a packing and crating service, subcontracted with TPS for TPS to provide packing and crating services for Walt Disney Company, one of GCP's major customers. *Id.* at 1132. TPS and GCP signed an in-term and post-term covenant not to compete, which provided that TPS

In *Kelton v. Stravinski,* the California Court of Appeal addressed another in-term covenant not to compete, this time in a partnership context. 138 Cal.App.4th at 945, 41 Cal.Rptr.3d 877.[16] The court held that even though the *Kelton-Stravinski* covenant not to compete was during an ongoing business relationship, it violated CBPC §16600 and was unenforceable. *Kelton,* 138 Cal.App.4th at 947, 41 Cal.Rptr.3d 877. The court in *Kelton* limited *Dayton Time Lock* to franchise agreements. However, in stressing CBPC §16600's strong policy against anti-competition agreements, the court reaffirmed that in the franchise context, §16600 prohibits an in-term covenant not to compete that "will foreclose competition in a substantial share of the affected line of commerce." *Kelton,* 138 Cal.App. 4th at 947-48, 41 Cal.Rptr.3d 877.

Dayton Time Lock and *Kelton* make evident that under CBPC §16600 an in-term covenant not to compete in a franchise-like agreement will be void if it "foreclose[s] competition in a substantial share" of

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would not work directly for, or solicit business from, Disney or any other company GCP introduced to TPS. *Id.* Although from the opinion it is unclear whether TPS and GCP's business relationship dissolved, we nonetheless upheld the covenant not to compete because it only limited the sub-contractor's "access to a narrow segment of the packing and shipping market." *Id.* at 1134. Because the covenant not to compete left a substantial portion of the packing and shipping market open to TPS, we held that the covenant not to compete was enforceable. *Id.*

[16] The covenant not to compete provided that *Kelton* agreed not to operate any warehouses and *Stravinski* agreed not to design or build any warehouses. *Kelton,* 138 Cal.App.4th at 945, 41 Cal.Rptr.3d 877.

a business, tradc, or market. *Dayton Time Lock,* 52 Cal.App.3d at 6, 124 Cal.Rptr. 678; *Kelton,* 138 Cal.App.4th at 948, 41 Cal.Rptr.3d 877. Also, California courts are less willing to approve in-term covenants not to compete outside a franchise context because there is not a need "to protect and maintain [the franchisor's] trademark, trade name and goodwill." *Kelton,* 138 Cal.App.4th at 948, 41 Cal.Rptr.3d 877. Keeping in min d these settled principles of California law that were set forth in *Dayton Time Lock* and reaffirmed by *Kelton,* which principles were expressly before the arbitrator, we proceed to evaluate whether the arbitrator's decision was in manifest disregard of the law.

CCI's "business" is operating full-service comedy clubs. CCI currently operates at least seven Improv clubs. *See supra* note 4. As interpreted by the arbitrator, the §9j covenant not to compete applies geographically to the contiguous United States, and does not end until 2019. Thus, the covenant not to compete has dramatic geographic and temporal scope. Combined with the arbitrator's ruling that CCI forfeited its rights to use the Improv marks license in any new location, the practical effect of the arbitrator's award enforcing §9j is that for more than fourteen years the entire contiguous United States comedy club market, except for CCI's current Improv clubs, is off limits to CCI. This "foreclose[s] competition in a substantial share" of the comedy club business. *Dayton Time Lock,* 52 Cal.App.3d at 6, 124 Cal.Rptr. 678; *see also Gen. Commercial,* 126 F.3d at 1134(reasoning that a contract cannot place "a substantial segment of the market off limits").

In ruling on CCI's motion for reconsideration the arbitrator reasoned as follows:

> *Dayton Time Lock* ... is inapplicable. That case involved an attack on an exclusive dealing contract under the *antitrust laws.* The cases cited in the portion of the *Dayton* opinion ... involved validity of exclusive dealing contracts under the federal Sherman Act. The type of "rule of reason" analysis applied in antitrust cases-involving the determination whether a particular agreement unreasonably restricts competition generally in a defined geographic and product market-is not applicable to a determination of illegality under Section 16600. California's antitrust statute, the Cartwright Act, is separate and distinct from §16600 of the Business & Professions Code.

The arbitrator's award, while aware of *Dayton Time Lock,* interpreted it in a way to render it inapplicable to this case. However, as we have explained, *Dayton Time Lock* established that under CBPC §16600 in-term covenants not to compete cannot prevent a party from engaging in its business or trade in a substantial section of the market. The arbitrator's award effectively quarantines CCI from engaging in its business in forty-eight states until 2019 and does not follow well-established California law. *See Dayton Time Lock,* 52 Cal.App.3d at 6, 124 Cal.Rptr. 678; *Great Frame Up Sys.,* 789 F.Supp. at 256; *see also Gen. Commercial,* 126 F.3d at 1134.

Even under the permissive standard with which we view arbitral decisions, the economic restraint of §9j. on competition is too broad to be countenanced in light of the clear prohibition of §16600, as interpreted by the California courts. The grounds given by the arbitrator for disregarding *Dayton Time Lock* are fundamentally incorrect.[17] We hold that the arbitrator's ruling that §9j is a valid covenant not to compete ignores CBPC §16600 and thus is in manifest disregard of the law. To comply with §16600, the covenant not to compete must be more narrowly tailored to relate to the areas in which CCI is operating Improv clubs under the license agreement.

However, we do not void the entire in-term covenant not to compete. *Kelton* stressed that the franchisor-franchisee context was different from an employment or partnership context. CCI's relationship with Improv West is in essence a

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[17] First, the arbitrator reasoned that *Dayton Time Lock* was inapplicable because it involved an assessment of antitrust laws. However, *Dayton Time Lock* made clear that it was assessing the requirements of CBPC §16600, and its plain language applied standards from antitrust cases in aid of its application of §16600. Second, the arbitrator thought §16600 was inapplicable because California in the Cartwright Act had a separate antitrust statute distinct from §16600, but the arbitrator's notice of the Cartwright Act does not detract from what *Dayton Time Lock* held in assessing an issue under §16600, which *Dayton Time Lock* itself characterized as a state antitrust law. Both §16600 and the Cartwright Act deal with antitrust and competition policy and it was not in the province of the arbitrator to make a "ruling" about §16600 that was so at odds with what the California Court of Appeal stated in *Dayton Time Lock*.

franchise agreement as CCI contracted with Improv West to use Improv West's trademarks and open comedy clubs modeled on Improv West's clubs. *See Kelton*, 138 Cal.App.4th at 947-48, 41 Cal.Rptr.3d 877 (discussing franchising under California law). Assessing the requirements of California law, we weigh CCI's right to operate its business against Improv West's interest "to protect and maintain its trademark, trade name and goodwill." *Id.* at 948, 41 Cal.Rptr.3d 877. This balance tilts in favor of Improv West with regard to counties where CCI is operating an Improv club, but under the restraint of CBPC §16600 California law does not permit an arbitrator to foreclose CCI's competition in opening comedy clubs throughout the United States.

Therefore, we hold that the district court should vacate the arbitrator's injunctive relief as to any county where CCI does not currently operate an Improv club, but uphold §9j in those counties where CCI currently operates Improv clubs. *See Armendariz v. Found. Health Psychcare Servs., Inc.*, 24 Cal.4th 83, 123, 99 Cal.Rptr.2d 745, 6 P.3d 669 (2000) (stating that "overbroad covenants not to compete may be restricted temporally and geographically" (citing *Gen. Paint Corp. v. Seymour*, 124 Cal.App. 611, 614-15, 12 P.2d 990 (1932))). Nationwide CCI may open and operate non-Improv comedy clubs in all those counties where it does not currently operate an Improv club. However, CCI may not open or operate any non-Improv clubs in those counties where it currently owns or operates Improv clubs.

IV

In sum, we hold that CCI's appeal of the district court's order compelling arbitration is untimely and we lack jurisdiction to consider that issue. We conclude (1) that the arbitrator properly arbitrated the equitable claims; (2) that the arbitrator's award is not completely irrational; (3) that the arbitrator exceeded the scope of his authority by enjoining the non-party Affiliates; and (4) that the arbitrator's award violates CBPC §16600. We vacate the district court's order confirming the arbitration award and remand to the district court with instructions to vacate the Partial Final Arbitration Award in so far as it enjoins CCI's Affiliates, unless they are agents or otherwise acting for CCI, and to the extent it prevents CCI from opening or operating non-Improv clubs in counties in which CCI does not now operate or own an Improv club.[18]

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[18] Improv West contends, without opposition from CCI, that the arbitration section in the Trademark Agreement entitles it to attorneys' fees and costs associated with this appeal and the confirmation proceedings of the arbitration awards. The arbitration agreement does award "costs, including reasonable attorneys fees" to "[t]he prevailing party." And we have upheld such an award for a party who successfully confirmed an arbitration award. *See A.G. Edwards & Sons, Inc. v. McCollough*, 967 F.2d 1401, 1404 (9th Cir. 1992) (per curiam) (ordering the arbitration award confirmed, and awarding the prevailing party "attorneys' fees in accordance with the agreements between the parties"). However, in this case Improv West partially confirmed the arbitrator's award, but we have modified the scope of that award. We hold that Improv West is entitled to costs and fees only with regard to its work on the issues on which it prevailed. We remand the issue of

AFFIRMED IN PART, VACATED IN PART, and REMANDED to the district court for further proceedings consistent with this opinion.

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costs and attorneys' fees to the district court to determine the amount of reasonable attorneys' fees and costs that should be awarded to Improv West insofar as it prevailed.

Appendix B

United States Court of Appeals, Ninth Circuit

NOS. 05-55739, 05-56100

COMEDY CLUB, INC., a Louisiana corporation; Al Copeland Investments, Inc., a Louisiana corporation,

Plaintiffs-Appellants,

v.

IMPROV WEST ASSOCIATES, a California Limited Partnership; California Comedy, Inc., a California corporation,

Defendants-Appellees.

Comedy Club, Inc., a Louisiana corporation; Al Copeland Investments, Inc., a Louisiana corporation,

Plaintiffs-Appellants,

v.

Improv West Associates, a California Limited Partnership; California Comedy, Inc., a California corporation,

Defendants-Appellees.

Sept. 7, 2007

OPINION

Before: JEROME FARRIS and RONALD M. GOULD, Circuit Judges, and KEVIN THOMAS DUFFY,* District Judge.

GOULD, Circuit Judge:

On June 13, 1999, Comedy Club, Inc. and Al Copeland Investments, Inc. (collectively "CCI") executed a Trademark License Agreement ("Trademark Agreement") with Improv West Associates ("Improv West") that granted CCI an exclusive nationwide license to use Improv West's trademarks. A few years later, CCI breached the agreement and sought to protect its interests in the trademarks in federal district court by filing a declaratory judgment action. After a complex procedural history, the parties were left with an arbitration award and two district court orders, one order compelling the parties to arbitrate, and another order confirming the arbitration award. CCI appeals both district court orders. We have jurisdiction under 28 U.S.C. §1291. We lack jurisdiction to review the district court's order compelling arbitration. We affirm in part and vacate in part the district court's order confirming the arbitration award, and we remand to the district court for further proceedings.

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* The Honorable Kevin Thomas Duffy, Senior United States District Judge for the Southern District of New York, sitting by designation.

I

Improv West is the founder of the Improv Comedy Club and the creator and owner of the "Improv" and "Improvisation" trademarks ("Improv marks"). CCI owns and operates restaurants and comedy clubs nationwide. On June 13, 1999, CCI and Improv West entered a Trademark Agreement[1] that provided, *inter alia*: (1) that Improv West granted CCI an exclusive nationwide license to use the Improv marks in connection with the opening of new comedy clubs; (2) that, according to a development schedule, CCI was to open four Improv clubs a year in 2001 through 2003;[2] and (3) that CCI was prohibited from opening any non-Improv comedy clubs during the term of the Trademark Agreement.[3] The Trademark Agreement also had an arbitration clause:

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[1] Also on June 13, 1999, in a separate Asset Purchase Agreement, CCI purchased the Melrose Improv Club from Improv West. The Melrose Improv Club is located in Los Angeles, California.

[2] The original §12.a. of the Trademark Agreement called for CCI to open and operate at least three Improv clubs by 2001, and two each year thereafter so that CCI would own and operate at least seven Improv clubs by 2003. CCI and Improv West amended §12.a. on October 19, 1999, creating the schedule of four Improv clubs a year in 2001 through 2003.

[3] Section 9.j. of the Trademark Agreement stated: "Licensee shall not own or operate, and Licensee shall ensure that none of its Affiliates shall own or operate any bar, restaurant, nightclub, or other facility which presents live stand-up or sketch comedy performances or live improvisational performances, other than the Melrose Improv or a Club, or Second City."

> All disputes relating to or arising under this Agreement or the Asset Purchase Agreement shall be resolved by arbitration in Los Angeles, California in accordance with the commercial arbitration rules of the American Arbitration Association. In any such arbitration, the parties shall be entitled to discovery in the same manner as if the dispute was being litigated in Los Angeles Superior Court. Notwithstanding this agreement to arbitrate, the parties, in addition to arbitration, shall be entitled to pursue equitable remedies and agree that the state and federal courts shall have exclusive jurisdiction for such purpose and for the purpose of compelling arbitration and/or enforcing any arbitration award. The parties agree to submit to the jurisdiction of such courts and agree that service of process in any such action may be made by certified mail. The prevailing party in any arbitration or action to enforce this Agreement or the Asset Purchase Agreement shall be entitled to its costs, including reasonable attorneys fees.

CCI concedes that it failed to open eight Improv clubs by 2002,[4] and that it was in default of amended §12.a. of the Trademark Agreement. Consistent with Improv West's sole remedy, as

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[4] In CCI's original complaint, CCI claims that it opened or obtained an interest in at least seven Improv clubs, not including the Melrose Improv Club.

stated in §13.b.,[5] Improv West sent CCI a letter asserting that CCI was in default of the Trademark Agreement, withdrawing CCI's license to use the Improv marks and rights to open more Improv clubs, and informing CCI that Improv West intended to begin opening its own Improv clubs.

In response to Improv West's letter, CCI filed a complaint in federal district court seeking declaratory relief. CCI's complaint sought a declaration that the covenant that CCI could not open any non-Improv comedy clubs was void under California Business and Professions Code ("CBPC") §16600, and that CCI's failure to meet the development schedule did not revoke CCI's license to the Improv marks or right to open Improv clubs. Improv West then filed a demand for arbitration seeking damages.[6]

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[5] Section 13.b. of the Trademark Agreement provided Improv West's sole remedy in the event CCI defaulted on the §12.a. development schedule. In pertinent part, §13.b. stated:

> Notwithstanding the above enumerated remedies, in the event [CCI] fails to fulfill the schedule set forth in section 12.a., [Improv West's] sole remedy shall be as follows. Upon notice to [CCI], [CCI] shall lose the right, power, and License (i) to use the Trademarks in connection with any Clubs which are not, as of the date of such failure, under construction or open for business and operated by [CCI], an Affiliate of [CCI] or other Operator and (ii) to sub-license Third Parties use of the Trademarks in connection with any new Clubs.

[6] In a further response, CCI amended its complaint seeking to enjoin Improv West from opening, or authorizing third parties to open, any Improv clubs, and asking for disgorgement of Improv West's profits from any such action.

On August 2, 2004, the district court ordered the parties to arbitrate their dispute. CCI did not appeal that order until May 16, 2005.

On February 28, 2005, the arbitrator entered a Partial Final Arbitration Award that stated: (1) that CCI defaulted on the Trademark Agreement by failing to adhere to the development schedule listed in amended §12.a.; (2) that CCI forfeited its rights to open Improv clubs and its use of the Improv marks license in connection with any clubs not open or under construction as of October 15, 2002; (3) that Improv West could open or license to third parties new Improv clubs; (4) that §9.j. of the Trademark Agreement was "a valid and enforceable in-term covenant not to compete" and remained valid "for the remaining term of the Agreement";[7] (5) that CCI and its "Affiliates"[8] were enjoined from opening or operating any other comedy clubs other than those open or under construction as of October 15, 2002 for the duration of the Trademark Agreement; (6) that

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[7] Unless the parties agree to terminate the Trademark Agreement earlier, by its own terms, the Trademark Agreement does not end until 2019.

[8] Section 1 of the Trademark Agreement stated, in relevant part, that "a 'Person'" is "any natural person, or any corporation, partnership, joint venture, limited liability company, business association, trust ... or other entity," and that the term "Affiliate" means and includes "any members of such Person's immediate family, or the member of the immediate family of any direct or indirect shareholder of such Person.... Further, the members of the immediate family of any Person shall include all collateral relatives of such Person having a common linear ancestor with such Person, and the spouse or any former spouse of such Person or any of such collateral relatives of such spouse."

neither CCI nor its Affiliates could change the name on any of its current clubs; and (7) that Improv West was entitled to attorneys fees and costs. On April 14, 2005, the district court confirmed the Partial Award. CCI timely appealed, tendering to us the issues addressed in this opinion.[9]

II

CCI first argues that the district court erred when it issued its order compelling the parties to arbitrate. Improv West in turn contends that we lack jurisdiction over this issue because CCI's appeal of the district court's order compelling arbitration is untimely.

The district court's order compelling the parties to arbitrate dismissed CCI's claims when it sent the parties to arbitration. Because the district court's order dismissed CCI's claims, it is a final order. *See Green Tree Fin. Corp. v. Randolph*, 531 U.S. 79, 86, 121 S.Ct. 513, 148 L.Ed.2d 373 (2000) (holding that a district court's order dismissing the plaintiff's claims and compelling arbitration was a final decision because the order "end[ed] the

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[9] Although all the issues in this appeal concern the arbitrator's decision in the Partial Final Arbitration Award entered on February 28, 2005, the arbitrator issued a second arbitral award, the Final Arbitration Award, which was decided on May 20, 2005. The district court confirmed that award on June 21, 2005, and entered judgment on August 29, 2005. CCI timely appealed the district court's order confirming the Final Arbitration Award on July 20, 2005, but raised no issues on appeal concerning that award. We consolidated the two cases for appeal purposes.

litigation on the merits and le[ft] nothing more for the court to do but execute the judgment" (internal quotation marks omitted)); *see also* 9 U.S.C. §16(a)(3) (2006) ("An appeal may be taken from ... a final decision with respect to an arbitration that is subject to this title."); 9 U.S.C. §16(a)(3) prac. cmt. (instructing that subdivision (a)(3) makes appealable a district court's determination compelling arbitration that is a final decision); *Bushley v. Credit Suisse First Boston*, 360 F.3d 1149, 1153 n. 1 (9th Cir. 2004) (adopting the principle that "a dismissal renders an order appealable under §16(a)(3)" (citation omitted)).

28 U.S.C. §2107(a) and Federal Rule of Appellate Procedure 4(a)(1) require that a notice of appeal be filed in a civil case "within 30 days after the judgment or order appealed from is entered." Fed. R.App. P. 4(a)(1)(A). Because the district court did not enter judgment on the order to compel arbitration, CCI had 180 days to appeal the order. *See* Fed. R.App. P. 4(a)(7)(A)(ii); *see also Bowles v. Russell*, --- U.S. ----, 127 S.Ct. 2360, 2363, 168 L.Ed.2d 96 (2007) (stating that "the taking of an appeal within the prescribed time is mandatory and jurisdictional" (internal quotation marks omitted)).

CCI filed its first notice of appeal of the district court's order compelling arbitration on May 16, 2005, 287 days after the order was entered on August 2, 2004. This is well beyond the 180 days allowed by Federal Rule of Appellate Procedure 4(a)(7)(A)(ii). CCI's appeal of the district court's order compelling arbitration is untimely, and we lack jurisdiction to hear the appeal of that issue.

III

We next consider CCI's contention that the district court erred by confirming the arbitration award. We review a district court's confirmation of an arbitration award de novo. *See First Options of Chi., Inc. v. Kaplan*, 514 U.S. 938, 947-48, 115 S.Ct. 1920, 131 L.Ed.2d 985 (1995). CCI presents four arguments: (1) that the arbitrator lacked authority to arbitrate the equitable claims; (2) that the arbitrator exceeded the scope of his authority by issuing two permanent injunctions; (3) that the arbitrator's award is irrational; and (4) that the arbitrator's award violates CBPC §16600. We address each argument in turn.

A

CCI submits that the arbitrator lacked authority to arbitrate because the arbitration clause in the Trademark Agreement grants state and federal courts an "exclusive" jurisdiction over equitable claims. We review the validity and scope of an arbitration clause de novo. *See Moore v. Local 569 of Int'l Bhd. of Elec. Workers*, 53 F.3d 1054, 1055-56 (9th Cir. 1995).

It is well established "that where the contract contains an arbitration clause, there is a presumption of arbitrability." *AT & Techs., Inc. v. Commc'ns Workers of Am.*, 475 U.S. 643, 650, 106 S.Ct. 1415, 89 L.Ed.2d 648 (1986). "[A]n order to arbitrate the particular grievance should not be denied unless it may be said with positive assurance that the arbitration clause is not susceptible of an

interpretation that covers the asserted dispute. Doubts should be resolved in favor of coverage." *Id.*; *see also Three Valleys Mun. Water Dist. v. E.F. Hutton & Co.*, 925 F.2d 1136, 1139 (9th Cir. 1991) ("Under the Federal Arbitration Act ... any doubts concerning the scope of arbitrable issues should be resolved in favor of arbitration ...." (internal quotation marks and citation omitted)).

It is also well established that "[w]hen deciding whether the parties agreed to arbitrate a certain matter ... courts generally ... should apply ordinary state-law principles that govern the formation of contracts." First Options, 514 U.S. at 944, 115 S.Ct. 1920. Only disputes "that the parties have agreed to submit to arbitration" should be arbitrated. *Id.* at 943, 115 S.Ct. 1920; *see also Republic of Nicar. v. Standard Fruit Co.*, 937 F.2d 469, 478 (9th Cir. 1991) (stating that "[t]he scope of the [arbitration] clause must ... be interpreted liberally").

Under California contract law, "if the language [of a contract] is clear and explicit, and does not involve an absurdity" the language must govern the contract's interpretation. Cal. Civ.Code §1638. Moreover, when a contract is written, "the intention of the parties is to be ascertained from the writing alone, if possible." Cal. Civ.Code §1639. "[I]f reasonably practicable" a contract must be interpreted as a whole, "so as to give effect to every part, ... each clause helping to interpret the other." Cal. Civ.Code §1641; *see also In re Affordable Hous. Dev. Corp.*, 175 B.R. 324, 329 (9th Cir. BAP 1994) ("California law provides that one phrase of a

contract should not be interpreted so as to render another phrase of the contract meaningless."). However, "[i]f a contract is capable of two different reasonable interpretations, the contract is ambiguous," *Oceanside 84, Ltd. v. Fid. Fed. Bank*, 56 Cal.App.4th 1441, 1448, 66 Cal.Rptr.2d 487 (1997), and under the federal presumption in favor of arbitration, an arbitrator would have jurisdiction to arbitrate claims. *See AT' & T Techs.*, 475 U.S. at 650, 106 S.Ct. 1415; *Three Valleys*, 925 F.2d at 1139.

Applying these principles, we conclude that the Trademark Agreement's arbitration clause grants the arbitrator authority over "all disputes" arising from the Trademark Agreement. There are three relevant clauses in the arbitration agreement: (1) "[a]ll disputes relating to or arising under this Agreement ... shall be resolved by arbitration"; (2) "[n]otwithstanding this agreement to arbitrate, the parties, in addition to arbitration, shall be entitled to pursue equitable remedies and agree that the state and federal courts shall have exclusive jurisdiction for such purpose and for the purpose of compelling arbitration and/or enforcing any arbitration award"; and (3) "[t]he prevailing party in any arbitration or action to enforce this Agreement ... shall be entitled to its costs, including reasonable attorneys fees."

CCI contends that clause two is explicit that only state and federal courts, and not an arbitrator, have jurisdiction over equitable claims. Improv West counters that the second clause only carved out equitable claims "in aid of arbitration" to maintain the status quo between the parties pending arbitration, and that the second clause did not

"supplant the arbitrator's authority" to decide all disputes under the Trademark Agreement.

A natural reading of clause two lends plausibility to Improv West's theory. The language "in addition to arbitration" in clause two suggests that arbitration still applies to all disputes, but that in addition, the parties are "entitled to pursue equitable remedies" before courts. If the parties intended to carve out an exception to arbitration for all equitable claims, they could have done so without the language "in addition to arbitration." Because the parties included this language, it is plausible and a permissible contract interpretation that the equitable claims exception in clause two was intended to apply only to claims designed to maintain the status quo between the parties. Stated another way, it was a rational interpretation of the agreement to say that the arbitrator could decide both equitable and legal claims and that the provision for court jurisdiction on equitable matters was ancillary to the arbitration. Moreover, the Federal Arbitration Act, 9 U.S.C. §3, provides a court with the ability to stay "trial of [an] action until such arbitration has been had," but it does not give a court the authority to issue equitable remedies, such as a temporary injunction, to maintain the status quo between the parties. Thus, it makes sense that if the parties wanted to give themselves the ability to seek temporary equitable remedies in courts while arbitration was ongoing, they would add such a clause to the arbitration agreement.

To support its interpretation, CCI cites language in clause three that awards costs and

attorneys fees to "the prevailing party in any arbitration or action to enforce this Agreement," and phrasing in clause two that grants exclusive jurisdiction to courts for the "purpose" of "equitable remedies." These phrases, although consistent with CCI's reading of the arbitration agreement, are equally consistent with Improv West's interpretation. These phrases can support that the arbitration agreement lets the parties pursue equitable remedies in courts in aid of the arbitration, and gives those courts exclusive jurisdiction over, and awards costs and attorneys fees to the prevailing party in, those actions.

We conclude that the arbitration agreement is "capable of two different reasonable interpretations." Oceanside 84, 56 Cal.App.4th at 1448, 66 Cal.Rptr.2d 487. Under the federal presumption in favor of arbitration, because the arbitration agreement is ambiguous, it should be interpreted as granting arbitration coverage over "all disputes" arising from the Trademark Agreement. *See AT & T Techs.*, 475 U.S. at 650, 106 S.Ct. 1415; *Three Valleys*, 925 F.2d at 1139. We hold that the arbitration agreement gave the arbitrator authority over all disputes, equitable and legal, and that he did not exceed his authority by arbitrating equitable claims.

B

We next address CCI's argument that the arbitrator exceeded the scope of his authority in issuing two permanent injunctions, which would provide grounds to vacate the arbitration award. *See*

Coutee v. Barington Capital Group, L.P., 336 F.3d 1128, 1134 (9th Cir. 2003); 9 U.S.C. §10(a)(4).

In his partial arbitration award, the arbitrator (1) enjoined CCI and its Affiliates from opening or operating any other comedy clubs other than those open or under construction as of October 15, 2002 for the duration of the Trademark Agreement and (2) enjoined CCI and its Affiliates from changing the name on any of their current clubs until the Trademark Agreement ended. CCI argues that because the Trademark Agreement defines Affiliates to include "family members, family members of shareholders, all collateral relatives,[10] former spouses, and all collateral relatives of former spouses," the permanent injunctions attempt to bind persons beyond the scope of the arbitrator's authority.[11] We agree.

A contract may bind non-parties such as an

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[10] Black's Law Dictionary defines "collateral relative" as "[a] relative who is not in the direct line of descent, such as a cousin." Black's Law Dictionary 1315 (8th ed. 2004).

[11] CCI raises this issue for the first time on appeal. Although we generally do "not consider an issue raised for the first time on appeal," we recognize three exceptions to that rule, by which we may invoke our discretion and review the issue: (1) where "review is necessary to prevent a miscarriage of justice or to preserve the integrity of the judicial process"; (2) where there is a change in the law creating a new issue; or (3) "when the issue presented is purely one of law and either does not depend on the factual record developed below, or the pertinent record has been fully developed." *Cold Mountain v. Garber*, 375 F.3d 884, 891 (9th Cir. 2004) (internal quotation marks and citation omitted). Here, we exercise our discretion and review CCI's argument under exceptions one and three.

intended third party beneficiary, an agent, or an assignee. *See Benasra v. Marciano*, 92 Cal.App.4th 987, 991, 112 Cal.Rptr.2d 358 (2001). But generally arbitration clauses and contracts do not bind non-parties in the absence of such extraordinary relationships. As explained in *Buckner v. Tamarin*, 98 Cal.App.4th 140, 119 Cal.Rptr.2d 489 (2002): "The strong public policy in favor of arbitration does not extend to those who are not parties to an arbitration agreement...." *Id.* at 142, 119 Cal.Rptr.2d 489 (internal quotation marks omitted); *see also NORCAL Mut. Ins. Co. v. Newton*, 84 Cal.App.4th 64, 76, 100 Cal.Rptr.2d 683 (2000) ("The common thread ... is the existence of an agency or similar relationship between the nonsignatory and one of the parties to the arbitration agreement. In the absence of such a relationship, courts have refused to hold nonsignatories to arbitration agreements.").

Here, the arbitrator's injunctions, relying on the Trademark Agreement's definition of Affiliate, seek to prevent people such as cousins of former spouses of CCI partners from opening or operating any comedy club within the United States until 2019. These collateral relatives are not in privity with the Trademark Agreement signatories, or with CCI shareholders, partners, or "persons." As an example, it is not reasonable to preclude from gainful competition in the comedy club sphere relatives of ex-spouses of the CCI principals who were not in an agency relationship with those principals. Similarly, the arbitrator did not have authority to enjoin a non-party grandmother of a CCI partner from opening a restaurant with live

stand-up comedy performance until the year 2019. Under California law, the arbitrator lacked the authority to enjoin these non-parties from owning or operating comedy-related businesses or restaurants.

Improv Vest contends that Federal Rule of Civil Procedure 65(d) ("Rule 65(d)") establishes that an injunction may bind not only parties to the action but also "their officers, agents, servants, employees, and attorneys, and [upon] those persons in active concert or participation with them." Fed.R.Civ.P. 65(d). However, the wholesale inclusion of relatives as Affiliates in the Trademark Agreement's covenant not to compete, and the injunctions in the arbitrator's partial award, go well beyond binding CCI's agents, employees, or people in active concert or participation with it as Rule 65(d) permits. Indeed, as mentioned above, §9.j., by its own terms, reaches beyond persons with an agency or assignee relationship with CCI partners, and literally purports to bind a CCI "person's" ex-wife and his ex-wife's cousins, nephews, uncles, and aunts. The text of Rule 65(d) is exclusive, stating that an injunction can permissibly bind "only" those persons listed in Rule 65(d). Rule 65(d) does not list collateral relatives of former spouses, or even grandparents, as potential non-parties who may be bound by a contract or an arbitration award. And we do not think it is a proper use of equitable power to restrain all such persons.

Moreover, precluding non-party relatives or ex-spouses from opening or operating improv-comedy-related businesses or restaurants violates CBPC §16600. CBPC §16600 provides, in relevant

part, that "every contract by which anyone is restrained from engaging in a lawful profession, trade, or business of any kind is to that extent void." *Id.* This is a codification of "the general rule in California [that] covenants not to compete are void." *Hill Med. Corp. v. Wycoff*, 86 Cal.App.4th 895, 901, 103 Cal.Rptr.2d 779 (2001). By restricting non-party relatives and ex-spouses from engaging in a lawful business, the injunctions, with respect to those persons, exceed the arbitrator's authority.

We conclude that the arbitrator acted beyond the scope of his authority as a matter of California law in attempting to bind all of CCI's Affiliates, including relatives who were not parties to the Trademark Agreement, and thus could not be bound by its provisions. If an arbitrator exceeded the scope of his authority in issuing an award, and that award is divisible, we may vacate part of the award and leave the remainder in force. *See Lyle v. Rodgers*, 18 U.S. (5 Wheat.) 394, 409, 5 L.Ed. 117 (1820) (Marshall, C.J.) (stating that "an award may be void in part, and good for the residue"); *Barington Capital*, 336 F.3d at 1134 ("A federal court may vacate an arbitration award, or a portion thereof, if the arbitrators acted beyond their authority."). We therefore conclude that the district court should vacate the arbitration award insofar as it enjoins any of CCI's Affiliates who are not connected to the principals of CCI as, by analogy to Rule 65(d), "their officers, agents, servants, employees, and attorneys, and [upon] those persons in active concert or participation with them." We hold that a narrowing of the restrictive covenant on Affiliates is required by CBPC §16600 and the principle that non-parties

generally are not bound in arbitration. Such non-parties can only be restrained to the extent permitted by Rule 65(d).

C

CCI next contends that the partial arbitration award is irrational because it simultaneously revokes CCI's license to open Improv clubs and prevents CCI from opening or operating any other comedy clubs anywhere in the United States until 2019 or the termination of the Trademark Agreement.

Review of an arbitration award is "'both limited and highly deferential'" and the arbitration award "may be vacated only if it is 'completely irrational' or 'constitutes manifest disregard of the law.'" *Poweragent Inc. v. Elec. Data Sys. Corp.*, 358 F.3d 1187, 1193 (9th Cir. 2004) (quoting Barington Capital, 336 F.3d at 1132-33). We have not elaborated on what "completely irrational" means, but the Eighth Circuit has persuasively indicated that the "completely irrational" standard is extremely narrow and is satisfied only "where [the arbitration decision] fails to draw its essence from the agreement." *Hoffman v. Cargill Inc.*, 236 F.3d 458, 461-62 (8th Cir. 2001). This is a view that we adopt.

Under the partial arbitration award, CCI lost its exclusive right to open and operate any new Improv clubs using Improv West's license. And because the arbitrator found the §9.j. covenant not to compete of the Trademark Agreement valid, CCI

also lost the right to open and operate any other new comedy clubs or restaurants under any other license or name anywhere in the contiguous United States as long as the Trademark Agreement remained in effect. Thus, apart from allowing CCI to continue to operate the handful of Improv clubs that it had already opened or purchased, see supra note 4, the arbitrator's ruling put CCI out of the comedy club business.

CCI argues that if it has lost all licensing rights, then there is no longer any licensing agreement. Both parties agree that if the Trademark Agreement is no longer in effect then the §9.j. covenant not to compete similarly would no longer be in effect, and the arbitrator's award would be considered irrational.

However, as Improv West correctly asserts, Improv West did not cancel the Trademark Agreement, neither party sought to terminate the Trademark Agreement as part of the underlying actions, and nothing in the parties' submissions, the arbitrator's rulings, or the district court's orders suggest that the Trademark Agreement was cancelled. Instead, CCI was still bound under other sections of the Trademark Agreement to pay Improv West royalties on the seven Improv clubs it still operated at the conclusion of the arbitration.

A breach by a party to a contract does not in itself cancel the contract.[12] Cancellation of a

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[12] The general rule is that if the breach is a material breach, it may give grounds for the non-breaching party to cancel the contract, *see Rano v. Sipa Press, Inc.*, 987 F.2d 580,

contract occurs when "either party puts an end to the contract for breach by the other."[13] *See* Bernard E. Witkin, *Summary of California Law* §925 (10th ed. 2005) (internal quotation marks omitted); *see also* Restatement (Second) of Contracts §274 (1979); 13 Arthur Linton Corbin, Corbin on Contracts §67.2 (Rev. ed. 2003).

At the time of arbitration, Improv West had not cancelled, nor had the parties terminated, the contract. In the arbitration Improv West did not seek to terminate the contract. By the arbitrator's own award, the arbitrator did not modify the party's contractual relationship, including the required payment of royalties, on the seven Improv clubs that CCI had opened or bought and was running. Further, per the arbitrator's award, the covenant not to compete ends when the Trademark Agreement ends. CCI will then be able to open up other non-Improv clubs.

CCI entered into the Trademark Agreement with knowledge that there would be consequences if it defaulted on the development schedule in §12.a. of the Trademark Agreement. An arbitrator could rationally decide that the §9.j. covenant not to compete was valid to some degree, while at the same

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586 (9th Cir. 1993), but if the breach is a partial breach, the non-breaching party's remedy is for damages. *See Postal Instant Press, Inc. v. Sealy*, 43 Cal.App.4th 1704, 1708-09, 51 Cal.Rptr.2d 365 (1996).

[13] "'Termination occurs when either party pursuant to a power created by agreement or law puts an end to the contract otherwise than for its breach.'" *See* Witkin, *Summary of California Law* §925 (internal quotation marks omitted).

time upholding Improv West's remedy to end CCI's exclusive license rights to open other Improv clubs.

The basic outline of what the arbitrator did, terminating an exclusive right to open Improv clubs nationwide, because of contractually inadequate performance contrary to the agreed schedule, while keeping in force the restrictive covenant makes sense insofar as CCI should not have an exclusive license on Improv clubs absent complying with designated performance. And so long as CCI was running some Improv clubs, a restrictive covenant to some degree could protect Improv West from damage caused by improper competition. Because we cannot say that there is no basis in the record for the arbitrator's decision, we hold that the arbitrator's award is not completely irrational. *See NF & M*, 524 F.2d at 760.

D

Finally, we address CCI's claim that the partial arbitration award should be vacated because it is in violation of CBPC §16600. CCI argues that the arbitrator's validation of §9.j. is in manifest disregard of the law. We have stated that for an arbitrator's award to be in manifest disregard of the law, "[i]t must be clear from the record that the arbitrator [ ] recognized the applicable law and then ignored it." *Mich. Mut. Ins. Co. v. Unigard Sec. Ins. Co.*, 44 F.3d 826, 832 (9th Cir. 1995).

Under CBPC §16600, it is well established that broad covenants not to compete are void unless they involve a situation where "a person sells the

goodwill of a business [or] where a partner agrees not to compete in anticipation of dissolution of a partnership," *see Kelton v. Stravinski*, 138 Cal.App.4th 941, 946, 41 Cal.Rptr.3d 877 (2006), CBPC §§16601, 16602, or "they are necessary to protect trade secrets." *Alliance Payment Sys. v. Walczer*, 61 Cal.Rptr.3d 789, 801 (2007). Neither party alleges any of the above exceptions apply in this case.

The majority of cases interpreting CBPC §16600 under California law deal with post-contract or post-employment covenants not to compete. *See, e.g., Alliance Payment Sys.*, 152 Cal.App.4th 620, 629, 61 Cal.Rptr.3d 789, 797; *Thompson v. Impaxx, Inc.*, 113 Cal.App.4th 1425, 1427-29, 7 Cal.Rptr.3d 427 (2003). In this case, the Trademark Agreement has not been terminated or canceled; rather the contractual relationship between CCI and Improv West is ongoing and §9.j. can be viewed as an in-term covenant not to compete.[14]

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[14] Because Improv West revoked CCI's rights to the Improv marks for almost the entire contiguous United States, the Improv West-CCI licensing relationship has ended except as to the existing Improv clubs. Bearing this in mind, it might be possible to view §9.j., with respect to the majority of the United States, functionally as if it were a post-term covenant not to compete, and with respect to the Improv clubs that CCI continues to operate, as an in-term covenant not to compete. However, because the contract relationship has not been canceled, and continues for the existing Improv clubs operated by CCI, we think it more appropriate conceptually to analyze §9.j. nationwide as an in-term covenant not to compete, while considering CCI's limited continuing use of the Improv marks as pertinent to the scope of §9.j.

We have not found, and the parties do not cite, any Ninth Circuit or California cases holding that in-term covenants not to compete of any scope are necessarily valid. There are, however, cases addressing in-term covenants not to compete, and we discuss several of those cases here because of the limitations that we believe they impose under §16600, even in the context of a continuing covenant not to compete.

Most significant to our analysis is *Dayton Time Lock Service, Inc. v. Silent Watchman Corp.*, 52 Cal.App.3d 1, 124 Cal.Rptr. 678 (1975), in which the California Court of Appeal, addressed an in-term "exclusive dealing clause" in a franchise agreement. *Id.* at 6, 124 Cal.Rptr. 678. The exclusive dealing clause provided in part that "during the life of this contract, ... [Dayton Time Lock Service, Inc. ("DTLS")] will not sell or lease any locks, devices or service of any kind in competition with the business of[Silent Watchman Corp. ("SW")], or use any time recording lock not supplied by [SW] under this agreement." *Id.* DTLS argued that this anti-competitive provision, along with a separate post-franchise covenant not to compete, violated state and federal antitrust laws. *Id.* The California Court of Appeal first noted that SW conceded that the post-term covenant not to compete violated the state antitrust law CBPC §16600. *Id.* Next, the court specifically addressed whether the in-term covenant not to compete was valid. In this context, the court held that "[e]xclusive-dealing contracts are not necessarily invalid," but "[t]hey are proscribed when it is probable that performance of the contract will foreclose competition in a substantial share of the

affected line of commerce." *Id.* In doing so, Dayton Time Lock imposed the standards analogous unto federal anti-trust law when interpreting §16600. *See id.* (*citing Standard Oil Co. v. United States*, 337 U.S. 293, 314, 69 S.Ct. 1051, 93 L.Ed. 1371 (1949)).[15]

In *Kelton v. Stravinski*, the California Court of Appeal addressed another in-term covenant not to compete, this time in a partnership context. 138

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[15] Similar to *Dayton Time Lock*, the District Court for the Northern District of Illinois in *Great Frame Up Systems, Inc. v. Jazayeri Enterprises*, 789 F.Supp. 253 (N.D.Ill. 1992), stated, while interpreting California law on CBPC §16600, that California courts support the position "that preventing defendants from competing only during the term of [an] existing franchise agreement, would not be void." *Id.* at 255. The court reasoned, however, that the in-term contractual provisions still cannot prevent a party from engaging in an entire profession, business or trade. *See id.* at 256.

Finally, in *General Commercial Packaging, Inc. v. TPS Package Engineering, Inc.*, 126 F.3d 1131 (9th Cir. 1997) (per curiam), we addressed a covenant not to compete in a general contractor-subcontractor context. General Commercial Packaging ("GCP"), a packing and crating service, subcontracted with TPS for TPS to provide packing and crating services for Walt Disney Company, one of GCP's major customers. *Id.* at 1132. TPS and GCP signed an in-term and post-term covenant not to compete, which provided that TPS would not work directly for, or solicit business from, Disney or any other company GCP introduced to TPS. *Id.* Although from the opinion it is unclear whether TPS and GCP's business relationship dissolved, we nonetheless upheld the covenant not to compete because it only limited the subcontractor's "access to a narrow segment of the packing and shipping market." *Id.* at 1134. Because the covenant not to compete left a substantial portion of the packing and shipping market open to TPS, we held that the covenant not to compete was enforceable. *Id.*

Cal.App.4th at 945, 41 Cal.Rptr.3d 877.[16] The court held that even though the *Kelton-Stravinski* covenant not to compete was during an ongoing business relationship, it violated CBPC §16600 and was unenforceable. *Kelton*, 138 Cal.App.4th at 947, 41 Cal.Rptr.3d 877. The court in *Kelton* limited *Dayton Time Lock* to franchise agreements. However, in stressing CBPC §16600's strong policy against anti-competition agreements, the court reaffirmed that in the franchise context, §16600 prohibits an in-term covenant not to compete that "will foreclose competition in a substantial share of the affected line of commerce." *Kelton*, 138 Cal.App.4th at 947-48, 41 Cal.Rptr.3d 877.

Dayton Time Lock and *Kelton* make evident that under CBPC §16600 an in-term covenant not to compete in a franchise-like agreement will be void if it "foreclose[s] competition in a substantial share" of a business, trade, or market. *Dayton Time Lock*, 52 Cal.App.3d at 6, 124 Cal.Rptr. 678; *Kelton*, 138 Cal.App.4th at 948, 41 Cal.Rptr.3d 877. Also, California courts are less willing to approve in-term covenants not to compete outside a franchise context because there is not a need "to protect and maintain [the franchisor's] trademark, trade name and goodwill." *Kelton*, 138 Cal.App.4th at 948, 41 Cal.Rptr.3d 877. Keeping in mind these settled principles of California law that were set forth in *Dayton Time Lock* and reaffirmed by *Kelton*, which

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[16] The covenant not to compete provided that *Kelton* agreed not to operate any warehouses and *Stravinski* agreed not to design or build any warehouses. *Kelton*, 138 Cal.App.4th at 945, 41 Cal.Rptr.3d 877.

principles were expressly before the arbitrator, we proceed to evaluate whether the arbitrator's decision was in manifest disregard of the law.

CCI's "business" is operating full-service comedy clubs. CCI currently operates at least seven Improv clubs. *See supra* note 4. As interpreted by the arbitrator, the §9.j. covenant not to compete applies geographically to the contiguous United States, and does not end until 2019. Thus, the covenant not to compete has dramatic geographic and temporal scope. Combined with the arbitrator's ruling that CCI forfeited its rights to use the Improv marks license in any new location, the practical effect of the arbitrator's award enforcing §9.j. is that for more than fourteen years the entire contiguous United States comedy club market, except for CCI's current Improv clubs, is off limits to CCI. This "foreclose[s] competition in a substantial share" of the comedy club business. *Dayton Time Lock*, 52 Cal.App.3d at 6, 124 Cal.Rptr. 678; *see also Gen. Commercial*, 126 F.3d at 1134 (reasoning that a contract can not place "a substantial segment of the market off limits").

In ruling on CCI's motion for reconsideration the arbitrator reasoned as follows:

> *Dayton Time Lock* ... is inapplicable. That case involved an attack on an exclusive dealing contract under the *antitrust laws*. The cases cited in the portion of the *Dayton* opinion ... involved validity of exclusive dealing contracts under the federal Sherman Act. The type of "rule of

> reason" analysis applied in antitrust cases-involving the determination whether a particular agreement unreasonably restricts competition generally in a defined geographic and product market-is not applicable to a determination of illegality under Section 16600. California's antitrust statute, the Cartwright Act, is separate and distinct from §16600 of the Business & Professions Code.

The arbitrator's award, while aware of *Dayton Time Lock*, interpreted it in a way to render it inapplicable to this case. However, as we have explained, *Dayton Time Lock* established that under CBPC §16600 in-term covenants not to compete cannot prevent a party from engaging in its business or trade in a substantial section of the market. The arbitrator's award effectively quarantines CCI from engaging in its business in forty-eight states until 2019 and does not follow well-established California law. *See Dayton Time Lock*, 52 Cal.App.3d at 6, 124 Cal.Rptr. 678; *Great Frame Up Sys.*, 789 F.Supp. at 256; *see also Gen. Commercial*, 126 F.3d at 1134. Even under the permissive standard with which we view arbitral decisions, the economic restraint of §9.j. on competition is too broad to be countenanced in light of the clear prohibition of §16600, as interpreted by the California courts. The grounds given by the arbitrator for disregarding *Dayton Time Lock* are fundamentally incorrect.[17] We hold that

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[17] First, the arbitrator reasoned that *Dayton Time Lock* was inapplicable because it involved an assessment of antitrust

the arbitrator's ruling that §9.j. is a valid covenant not to compete ignores CBPC §16600 and thus is in manifest disregard of the law. To comply with §16600, the covenant not to compete must be more narrowly tailored to relate to the areas in which CCI is operating Improv clubs under the license agreement.

However, we do not void the entire in-term covenant not to compete. *Kelton* stressed that the franchisor-franchisee context was different from an employment or partnership context. CCI's relationship with Improv West is in essence a franchise agreement as CCI contracted with Improv West to use Improv West's trademarks and open comedy clubs modeled on Improv West's clubs. *See Kelton*, 138 Cal.App.4th at 947-48, 41 Cal.Rptr.3d 877 (discussing franchising under California law). Assessing the requirements of California law, we weigh CCI's right to operate its business against Improv West's interest "to protect and maintain its

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laws. However, *Dayton Time Lock* made clear that it was assessing the requirements of CBPC §16600, and its plain language applied standards from antitrust cases in aid of its application of §16600, which was an issue under review. Second, the arbitrator thought §16600 was inapplicable because California in the Cartwright Act had a separate antitrust statute distinct from §16600, but the arbitrator's notice of the Cartwright Act does not detract from what *Dayton Time Lock* held in assessing an issue under §16600, which *Dayton Time Lock* itself characterized as a state antitrust law. Both §16600 and the Cartwright Act deal with antitrust and competition policy and it was not in the province of the arbitrator to make a "ruling" about §16600 that was so at odds with what the California Court of Appeal stated in *Dayton Time Lock*.

trademark, trade name and goodwill." *Id.* at 948, 41 Cal.Rptr.3d 877. This balance tilts in favor of Improv West with regard to counties where CCI is operating an Improv club, but under the restraint of CBPC §16600 California law does not permit an arbitrator to foreclose CCI's competition in opening comedy clubs throughout the United States.

Therefore, we hold that the district court should vacate the arbitrator's injunctive relief as to any county where CCI does not currently operate an Improv club, but uphold §9.j. in those counties where CCI currently operates Improv clubs. *See Armendariz v. Found. Health Psychcare Servs., Inc.*, 24 Cal.4th 83, 123, 99 Cal.Rptr.2d 745, 6 P.3d 669 (2000) (stating that "overbroad covenants not to compete may be restricted temporally and geographically" (*citing Gen. Paint Corp. v. Seymour*, 124 Cal.App. 611, 614-15, 12 P.2d 990 (1932))). Nationwide CCI may open and operate non-Improv comedy clubs in all those counties where it does not currently operate an Improv club. However, CCI may not open or operate any non-Improv clubs in those counties where it currently owns or operates Improv clubs.

IV

In sum, we hold that CCI's appeal of the district court's order compelling arbitration is untimely and we lack jurisdiction to consider that issue. We conclude (1) that the arbitrator properly arbitrated the equitable claims; (2) that the arbitrator's award is not completely irrational; (3) that the arbitrator exceeded the scope of his

authority by enjoining the non-party Affiliates; and (4) that the arbitrator's award violates CBPC §16600. We vacate the district court's order confirming the arbitration award and remand to the district court with instructions to vacate the Partial Final Arbitration Award insofar as it enjoins CCI's Affiliates, unless they are agents or otherwise acting for CCI, and to the extent it prevents CCI from opening or operating non-Improv clubs in counties in which CCI does not now operate or own an Improv club.[18]

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[18] Improv West contends, without opposition from CCI, that the arbitration section in the Trademark Agreement entitles it to attorneys' fees and costs associated with this appeal and the confirmation proceedings of the arbitration awards. The arbitration agreement does award "costs, including reasonable attorneys fees" to "[t]he prevailing party." And we have upheld

AFFIRMED IN PART, VACATED IN PART, and REMANDED to the district court for further proceedings consistent with this opinion.

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such an award for a party who successfully confirmed an arbitration award. *See A.G. Edwards & Sons, Inc. v. McCollough*, 967 F.2d 1401, 1404 (9th Cir. 1992) (per curiam) (ordering the arbitration award confirmed, and awarding the prevailing party "attorneys' fees in accordance with the agreements between the parties"). However, in this case Improv West partially confirmed the arbitrator's award, but we have modified the scope of that award. We hold that Improv West is entitled to costs and fees only with regard to its work on the issues on which it prevailed. We remand the issue of costs and attorneys' fees to the district court to determine the amount of reasonable attorneys' fees and costs that should be awarded to Improv West insofar as it prevailed.

Appendix C

United States District Court for the Central District of California

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Case No. CV-03-8134 WMB (AJWx)

COMEDY CLUB, INC., a Louisiana corporation; Al Copeland Investments, Inc., a Louisiana corporation,

Plaintiffs

v.

IMPROV WEST ASSOCIATES, a California Limited Partnership; California Comedy, Inc., a California corporation,

Defendants

April 12, 2005

ORDER CONFIRMING ARBITRATION AWARD

I. FACTS

Defendant Improv West ("Improv West") is the founder of the Improv Comedy Club on Melrose Avenue and the creator and owner of the Improv and Improvisation trademarks ("Improv marks"). Plaintiff Comedy Club, Inc. ("CCI") owns and operates restaurants and comedy clubs nationwide. In 1993, CCI and Improv entered into an Asset Purchase and Sale Agreement ("Asset Agreement")

and a Trademark License Agreement ("Trademark Agreement"). The Asset Agreement transferred ownership of the Melrose Improv Club to CCI. The Trademark Agreement provided for the following: (1) CCI was authorized to open additional Improv clubs and was granted an exclusive nationwide license to use the Improv marks in connection with these new clubs; (2) pursuant to a development schedule, CCI was to open four Improv clubs in 2001, four Improv clubs in 2002, and four Improv clubs in 2003; (3) CCI was prohibited from opening non-Improv comedy clubs; and (4) any dispute arising under the agreement was to be resolved through arbitration.

When CCI failed to open eight Improv clubs by 2002, Improv West sent CCI a letter holding CCI in default of the Trademark Agreement and "reserving" (i.e. withdrawing) CCI's rights to construct additional Improv clubs or use the Improv marks in connection with these new clubs. Improv West further informed CCI that Improv West intended to begin opening its own Improv clubs.

B. Procedural History

On November 7, 2003, after receiving Improv West's letter, CCI filed a complaint seeking declaratory relief. CCI sought a declaration that the covenant not to build non-Improv comedy clubs was void pursuant to Cal. Bus. & Prof. Code §16600. CCI also sought an affirmation that CCI had the exclusive right to open Improv clubs and that CCI's failure to meet the development schedule did not cause it to forfeit this right.

On March 5, 2004, Improv West made a demand for arbitration, alleging that CCI breached the Trademark Agreement by failing to meet the established schedule of opening eight clubs by 2002. Improv West's demand sought to establish its rights under the Trademark Agreement and to recover $150,000 in damages. Improv West amended this demand on April 6, 2004, to allege additional breaches of the Trademark Agreement.[1]

CCI thereafter amended its complaint to seek equitable as well as declaratory relief. The amended complaint alleged that Improv West had authorized third parties to infringe upon territory reserved to CCI under the Trademark Agreement. In connection with these new allegations, CCI sought a permanent injunction prohibiting Improv West from opening, or authorizing third parties to open, any clubs in CCI's exclusive territory, and requiring Improv West to disgorge any profits resulting from its breach of the Trademark Agreement.

Improv West moved to dismiss CCI's complaint for declaratory judgment, or, in the alternative, stay CCI's action pending arbitration. CCI opposed the motion, contending that the parties

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[1] According to the amended demand, CCI breached the Trademark Agreement by failing to meet the development schedule, failing to furnish Improv West with certified and complete financial statements, and commencing an action for declaratory judgment rather than arbitrating. CCI also anticipatorily breached the agreement by announcing their intent to change the names of their existing Improv clubs and announcing their intent to open new clubs under different names.

arbitration agreement contained a carve-out for actions seeking equitable remedies, and that its complaint was such an action. On July 28, 2004, the Court issued an order compelling the parties to arbitrate their dispute. Following the Court's ruling, the parties arbitrated before Richard R. Mainland.

During arbitration, the parties filed cross-motions for summary judgment on the two issues raised in CCI's complaint for declaratory judgment: (1) whether the non-compete clause was null and void, and (2) whether CCI's failure to open the requisite number of Improv clubs constituted a forfeit of its exclusivity rights under the Trademark Agreement. On September 7, 2004, the arbitrator issued an order ruling that the non-compete clause was valid and that CCI had forfeited its exclusivity rights. Shortly thereafter, CCI filed a motion for reconsideration in regards to the arbitrator's ruling on the non-compete clause. The arbitrator denied the motion.

On November 8, 2004, CCI filed a second amended counterclaim in which it sought repayment of certain license fees that it had pre-paid to Improv West. The counterclaim also sought an accounting and remuneration of amounts underpaid in regards to Improv West's alleged agreement to pay royalties to CCI for entertainment booking handled by CCI for Improv West.

On February 28, 2005, the arbitrator entered a partial final arbitration award stating, in part, that: (1) CCI had forfeited its right to use and license the Improv trademark in connection with any

clubs that were not open or under construction as of October 15, 2002; (2) Improv West was entitled to open or license new Improv clubs in territory that had been exclusively licensed to CCI; (3) during the duration of the Trademark Agreement, which runs until 2019, CCI was enjoined from operating any comedy clubs other than those that were open or under construction prior to October 15, 2002, or any club authorized by Improv West; (4) CCI was enjoined from changing the name of any of its current stand-up clubs until 2019; (5) Improv West was entitled to attorney's fees and costs. The award did not "decide [CCI's] booking-fee claim... which remains pending." *See* Arb. Rec., Ex. 126 at 3. The arbitrator characterized the booking-fee claim as "a separate and independent claim." *Id.* On March 4, 2005, Improv West filed a motion to confirm the arbitration award. CCI opposes the motion.

II. DISCUSSION

CCI argues that the arbitration award should not be confirmed for four reasons: (1) the issues raised in arbitration were equitable in nature and therefore were not arbitrable; (2) the booking-fee claim has not been resolved, thereby rendering the arbitrator's award non-final; (3) the arbitrator's decision regarding the non-compete clause was irrational or evidenced a manifest disregard for the law; (4) the arbitrator engaged in misconduct by sua sponte awarding injunctive relief.

A. Did the arbitrator have jurisdiction to hear equitable claims

CCI argues that the arbitrator did not have jurisdiction to hear the claims that were before it. Section 22 of the Trademark Agreement says that:

> All disputes arising under this Agreement ... shall be revised by arbitration in Los Angeles, California ... Notwithstanding this agreement to arbitrate, the parties, in addition to arbitration, shall be entitled to pursue equitable remedies and agree that the state and federal courts shall have exclusive jurisdiction for such purpose.

CCI contends that during the arbitration, the parties sought and were awarded remedies that were entirely equitable in nature. Therefore, CCI believes that under the terms of section 22, these claims could only be properly adjudicated in state or federal court.

CCI raised this exact same argument in opposition to Improv West's motion to compel arbitration. This Court rejected the argument, ruling that:

> [The] "equitable remedies" language in the arbitration provision should be interpreted to be limited to interim judicial relief necessary to preserve the status quo or judicial relief necessary to enforce an arbitrator's decision. As neither of CCI's requested relief, a

> permanent injunction or disgorgement of profits, constitutes interim relief or relief necessary to enforce an arbitrator's decision, arbitration of CCI's claim is appropriate.

See Order Sending Parties to Arbitration at 9 (July 28, 2004). The Court listed three reasons in support of its decision: (1) "this result is most consistent with the language of the provision and the intent of the parties," *id.*; (2) "Federal policy ... supports sending the parties to arbitration," *id.*; (3) "exercising judgment over CCI's claims for a permanent injunction and disgorgement of profits would create parallel and distinctive proceedings and carry the risk of inconsistent adjudications," *id.* at 10.

CCI argues that the Court should reconsider its order of July 28th in light of subsequent actions taken by Improv West. At the time the Court entered its July 28th ruling, Improv West was seeking monetary damages and injunctive relief. CCI alleges that during the arbitration, Improv West abandoned its claims for monetary damages, meaning that all of its remaining claims were equitable in nature. CCI contends that Improv West's actions have undermined the Court's third reason for compelling arbitration; i.e., that to do otherwise would result in duplicate proceedings.

Even assuming that neither party presented any legal claims presented during arbitration,[2] CCI's

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[2] Improv West alleges that CCI itself sought monetary damages in the arbitration. To the extent that this is true, it

argument overlooks the two additional reasons the Court gave in support of its decision to send the parties to arbitration. Specifically, the Court found that compelling arbitration was appropriate based on (1) the plain language of the arbitration agreement, and (2) federal policy. The Court affirms its prior ruling. Because CCI was not seeking interim relief or relief necessary to enforce the arbitrator's decision, arbitration of CCI's claims was appropriate.

B. Can the award be confirmed before the booking-fee issue is decided

CCI contends that the arbitration award cannot be confirmed because the arbitrator has not yet decided the booking-fee issue. In its second amended counterclaim, CCI claimed that Improv West owed it a booking-fee with respect to six Improv clubs operated by Improv West and/or its licensees. The arbitrator specifically declined to rule on the booking-fee issue in its partial final arbitration award and the issue is still pending.

CCI contends that this Court cannot confirm the arbitration award until every claim submitted to arbitration has been decided. As stated by the Sixth Circuit, "[t]his argument overlooks the rule that an interim award that finally and definitively disposes of a separate independent claim may be confirmed notwithstanding the absence of an award that finally disposes of all the claims that were submitted to

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completely undermines CCI's argument because it means that both legal and equitable claims remained in the case.

arbitration." *Island Creek Coal Sales Co. v. City of Gainsville*, 729 F.2d 1046, 1049 (6th Cir. 1984) (citing *Eurolines Shipping Co. v. Metal Transport Corp.*, 491 F.Supp. 590, 592 (S.D.N.Y. 1980), *Sperry Int'l Trade. Inc. v. Gov't of Israel*, 689 F.2d 301 (2d Cir. 1982); *Sportswear Garment Workers' Union, Local 246 v. Evans Mfg Co.*, 318 F.2d 528 (3d Cir. 1963)). This rule finds support in other circuits. *See Metallgesellschaft AG v. M/V Capitan Constante*, 790 F.2d 280, 283 (2d Cir. 1986); *see also Hart Surgical. Inc. v. Ultracision, Inc.*, 244 F.3d 231 (1st Cir. 2001).

The Ninth Circuit has never reviewed the rule enunciated by the Sixth Circuit. However, CCI argues that two Ninth Circuit cases have effectively rejected that holding. In the first case, *Millmen Local 550 v. Wells Exterior Trim*, 828 F.2d 1373 (9th Cir. 1987), a labor arbitrator determined the issue of liability in favor of the petitioner, but reserved jurisdiction to determine the remedy in some future proceeding. The Ninth Circuit held that the arbitrator's decision was not reviewable because "an arbitration award that postpones the determination of a remedy [is not] a 'final and binding award.'" *Id.* at 1376. In the second case, *Sunshine Mining Co. v. United Steelworkers*, 823 F.2d 1289 (9th Cir. 1987), an arbitrator premised an award on the outcome of a psychiatric test. The psychiatric test was never completed, but the district court reviewed the award and entered judgment. The Ninth Circuit ruled that the district court had erred, holding mat "inasmuch as the psychiatric examination ordered by the arbitrator in this case was never conducted, the instant award is incomplete ... The case must be

remanded to arbitration for a final and complete determination of the issue submitted." *Id.* at 1295. Neither *Wells Exterior* nor *Sunshine* involved claims that were finally disposed of in the arbitration: in the former case no remedy was issued and in the latter case the predicate event that was to trigger the arbitration award never occurred. In this case, the arbitrator simply severed one claim, which will be resolved at a later date.

Although the Ninth Circuit has never specifically endorsed the rule enunciated by the Sixth Circuit, this Court believes it is a sound one. Furthermore, CCI has not cited, nor is this Court aware of, any case that has rejected the rule. The Court therefore holds that the arbitrator's partial final award may be confirmed despite the fact that it did not resolve every single issue raised in the arbitration.

C. Was the arbitrator's decision irrational

CCI argues that the arbitrator's refusal to invalidate the non-compete clause must be set aside. Under the Federal Arbitration Act, a court's review of an arbitrator's decision is extremely narrow. As stated by the Ninth Circuit, when reviewing an arbitration award, courts must remain

> mindful that confirmation is required even in the face of erroneous misinterpretations of law. It is not even enough that the [arbitrator] may have failed to understand or apply the law. An arbitrator's decision must be upheld unless it is completely

> irrational, or it constitutes a manifest disregard of law.

Todd Shipyards Corp. v. Cunard Line, 943 F.2d 1056, 1059-60 (9th Cir. 2003). In order to overturn an arbitrator's award, "[i]t must be clear from the record that the arbitrator recognized the applicable law and then ignored it." *Mich. Mut. Ins. Co. v. Unigard Sec. Ins. Co.*, 44 F.3d 826, 832 (9th Cir. 1995).

In this case the arbitrator found that the parties non-compete agreement did not violate Cal. Bus. & Prof. Code §16600, which provides, that "except as provided in this chapter, every contract by which anyone is retrained from engaging in a lawful profession, trade or business of any kind is to that extent void." The arbitrator began by noting that "it has been held that Section 16600 applies only to covenants preventing one from engaging in an entire business, trade or profession." *See* PI.'s Reply, Ex. A at 5 (citing *Campbell v. Bd. of Trs. of Stanford Univ.*, 817 F.2d 499, 502 (9th Cir. 1987)). The arbitrator then interpreted the CCI/Improv West Trademark Agreement to mean that the non-compete clause would end when the Agreement expired. Based on this interpretation, the arbitrator ruled that the non-compete covenant was enforceable because it was "in-term," meaning that it only applied during the duration of the Trademark Agreement and was therefore only a partial restraint. This outcome finds support in the case law. As one Illinois district court found, "California courts draw a distinction between in-term restrictions and post-term restrictions, finding the latter and not the former

void under §16600. Using this reasoning, the restriction at issue here, preventing defendants from competing only during the term of the existing franchise agreement, would not be void." *Great Frame Up Sys., Inc. v. Jazayeri Enters., Inc.*, 789 F.Supp 253, 255-56 (N.D. Ill. 1992).

After the arbitrator issued its ruling, CCI filed a motion for reconsideration, arguing that courts should apply a "rule of reason" analysis when evaluating the enforceability of a non-compete clause. The arbitrator ruled that California courts have rejected a "rule of reason" in the context of non-competes. This ruling also finds support in the case law. *General Commercial Packaging, Inc. v. TPS Package Eng'g, Inc.*, 126 F.3d 1131, 1133 (9th Cir. 1997) ("the [Ninth Circuit has] disclaimed a rule of reason"). The arbitrator in this case spent several pages explaining its position in regards to the non-compete clause. Regardless of whether the arbitrator's ruling was, as a matter of law, correct or incorrect, it was not irrational.[3]

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[3] CCI also argues that the arbitrator committed misconduct when he refused to hear evidence on the effect that the non-compete clause would have on CCI's business. *See* 9 U.S.C. §10(a)(3) (permitting district court to vacate arbitration award "where the arbitrators were guilty of misconduct in refusing to ... hear evidence pertinent and material to the controversy"). CCI's argument is unpersuasive. The arbitrator in this case decided that California courts have rejected a "rule of reason" analysis in the context of non-competes. This ruling, which was not irrational, rendered CCI's evidence immaterial. Therefore, the arbitrator did not commit any misconduct.

D. Did the arbitrator commit misconduct

Finally, CCI argues that the arbitrator engaged in misconduct by sua sponte awarding Improv West injunctive relief. There are two problems with CCI's argument. First, the arbitrator's grant of injunctive relief was not sua sponte. The record indicates that prior to the arbitrator's entry of its final award, Improv West had repeatedly requested injunctive relief. *See, e.g.*, Arb. Rec., Ex. 82, 112, 113. Second, even if Improv West had not sought such relief, CCI has not cited any case law or other authority that says the sua sponte award of injunctive relief constitutes "misconduct" under 9 U.S.C, §10(a)(3). The arbitrator's grant of injunctive relief does not warrant vacation of the arbitration award.

III. CONCLUSION

Defendant's motion to confirm the arbitration award is granted.

IT IS SO ORDERED.

Dated: April 12, 2005

Wm. Matthew Byrne, Jr.
United States District Judge

Appendix D

United States District Court for the Central District of California

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Case No. CV 03-8134 WMB (AJWx)

COMEDY CLUB, INC., a Louisiana corporation; Al Copeland Investments, Inc., a Louisiana corporation,

Plaintiffs,

v.

IMPROV WEST ASSOCIATES, a California Limited Partnership; California Comedy, Inc., a California corporation,

Defendants.

May 4, 2005

JUDGMENT

The Motion to Confirm Arbitration Award filed by Defendants-Petitioners Improv West Associates and California Comedy, Inc. ("Petitioners") came before this Court for hearing on April 6, 2005, before the Honorable Wm. Matthew Byrne, Jr., in Courtroom 9 of the United States District Court. Based on the papers submitted in favor of and in opposition to the motion, the files and records in this action, all matters brought to the attention of the Court before its decision, and

matters of which the Court may take judicial notice, and further to its Order Confirming Arbitration Award dated April 12, 2005, and entered April 14, 2005, the Court orders and enters judgment as follows:

IT IS ORDERED THAT the Partial Final Arbitration Award of the Arbitrator dated February 25, 2005, including all awards of monetary, declaratory, and injunctive relief therein, be and the same hereby is CONFIRMED pursuant to the Federal Arbitration Act, 9 U.S.C. §9.

IT IS FURTHER ORDERED THAT Plaintiffs-Respondents Comedy Club, Inc. and Al Copeland Investments, Inc. ("Respondents") shall pay to Petitioners pre-judgment interest of five percent (5%) per annum, pursuant to Cal. Civ. Code §3287, on the monetary component of the Partial Final Arbitration Award through April 6, 2005, in the amount of $2,060.34.

IT IS FURTHER ORDERED THAT Respondents shall pay to Petitioners post-judgment interest pursuant to 28 U.S.C. §1961 from the date of this Judgment through the date of payment of the monetary portion of the Partial Final Arbitration Award.

Dated: May 4, 2005

Hon. Wm. Matthew Byrne, Jr.
United States District Judge

Appendix E

United States District Court for the Central District of California

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Case No. CV 03-8134 WMB (AJWx)

COMEDY CLUB, INC., a Louisiana corporation; Al Copeland Investments, Inc., a Louisiana corporation,

Plaintiffs,

v.

IMPROV WEST ASSOCIATES, a California Limited Partnership; California Comedy, Inc., a California corporation,

Defendants.

Aug. 25, 2006

JUDGMENT CONFIRMING FINAL ARBITRATION AWARD

Based on the papers submitted in favor of and in opposition to the Motion to Confirm Arbitration Award filed by Defendants-Petitioners Improv West Associates and California Comedy, Inc. ("Petitioners"), .the files and records in this action, all matters brought to the attention of the Court before its decision, and matters of which the Court may take judicial notice, and in accordance with the Stipulation And Order Re Confirmation Of Final Arbitration Award, Preservation of Arguments

Pending Appeal, And Stay Of Judgment Pending Appeal filed by the parties and entered by the Court, the Court orders and enters judgment as follows:

IT IS ORDERED THAT the Final Arbitration Award of the Arbitrator dated May 20, 2005 be and the same hereby is CONFIRMED pursuant to the Federal Arbitration Act, 9 U.S.C. §9.

IT IS FURTHER ORDERED THAT Respondents shall pay to Petitioners post-judgment interest pursuant to 28 U.S.C. §1961 from the date of this Judgment through the date of payment of the monetary portion of the Final Arbitration Award.

Dated: Aug. 25, 2006 _____

Hon. Wm. Matthew Byrne, Jr.
United States District Judge

Appendix F

American Arbitration Association

Case No.: 72 181 00274 04 NADE

IMPROV WEST ASSOCIATES and CALIFORNIA COMEDY, INC.,

Claimants,

v.

COMEDY CLUB, INC. and AL COPELAND INVESTMENTS, INC.,

Respondents.

May 20, 2005

FINAL ARBITRATION AWARD

THE UNDERSIGNED ARBITRATOR, having been designated In accordance with Section 22 of the Trademark License Agreement among the parties dated Juno 13, 1999, as amended (the "Agreement"), and having been duly sworn, having duly heard the proofs and allegations of the Parties, and Respondents having withdrawn their counterclaim respecting booking fees, and having previously rendered a Partial Final Arbitration Award dated February 25, 2005, does hereby issue this FINAL AWARD as follows;

1. The arbitrator previously issued a Partial Final Award dated February 25, 2005 (the "Partial Final Award"), which decided all claims submitted for decision, except for Respondent's booking fee claim alleged in paragraphs 5-7 of the Second Amended Counterclaim. In the Partial Final Award the arbitrator expressly retained jurisdiction to determine the booking fee claim and to allocate among the parties the administrative fees of the American Arbitration Association ("Association") and the fees of the arbitrator.

2. The parties have advised the arbitrator that Respondents' booking fee claim alleged in the Second Amended Counterclaim has been dismissed without prejudice and notice has been duly given to the parties of such dismissal. Accordingly, no decision will be made respecting that counterclaim.

3. Claimants are the prevailing parties in this matter and are entitled to recover all administrative fees of the Association and arbitrators' fees deposited by Claimants with the Association, except for such administrative and arbitrator's fees attributable to booking fee counterclaim, as to which there is no prevailing party. All administrative and arbitrator fees attributable to the booking fee counterclaim are to be borne by each party on a 50/50 basis.

4. Based on the findings in paragraph 3 above, the administrative fees of the Association and arbitrators' fees shall be borne as follows:

The administrative fees of the Association

totaling $3,600.00 shall be borne by Respondents, in that none of such fees related to the dismissed booking fee counterclaim. The compensation of the arbitrator totaling $42,237.00 and the expenses of the Arbitrator totaling $463.53 shall be borne as follows: All of these fees and costs are to be borne by Respondents, except that arbitrators' fees in the amount of $1,600.00 relate to the booking fee counterclaim and shall be borne equally by both patties. Therefore, the compensation and expenses of the Arbitrator totaling $42,700,53 shall be borne $800.00 by Claimants and $41,900.53 by Respondents. Pursuant to these findings, Respondents shall pay to Claimants the sum of Twenty-Two Thousand Nine Hundred Fifty Dollars and Twenty-Nine Cents ($22,950.29), representing its share of amounts previously advanced to the Association. These amounts reflect all payments made to date.

5. The amounts awarded herein are separate from and in addition to any amounts awarded pursuant to the Partial Final Award.

6. This Award and the Partial Final Award decide all claims submitted to the arbitrator for decision. Any claims, contentions or defenses not mentioned in this Award or the Partial Final Award are hereby denied.

Dated: May 20, 2005

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Richard R. Mainland
Arbitrator

Appendix G

American Arbitration Association

Case No.: 72 181 00274 04 NADE

IMPROV WEST ASSOCIATES and CALIFORNIA COMEDY, INC.,

Claimants,

v.

COMEDY CLUB, INC. and AL COPELAND INVESTMENTS, INC.,

Respondents.

Feb. 25, 2005

PARTIAL FINAL ARBITRATION AWARD

THE UNDERSIGNED ARBITRATOR, having been designated in accordance with Section 22 of the Trademark License Agreement among the parties dated June 13, 1999, as amended (the "Agreement"), and having been duly sworn, and having duly heard the proofs and allegations of the Parties, does hereby issue this PARTIAL FINAL AWARD as follows:

For the reasons set forth in the Arbitrator's Orders dated September 7, 2004, October 22, 2004, January 31, 2005, and February 17, 2005, the Arbitrator finds and awards as set forth below. Except as otherwise defined, capitalized terms in this Award shall have the meanings set forth in the Agreement.

1. Respondents Comedy Club, Inc. and Al Copeland Investments, Inc. ("Respondents") failed to fulfill the development schedule under the Agreement, and such failure was not excused;

2. Claimants Improv West Associates and California Comedy, Inc. ("Claimants") were entitled to exercise the remedy set forth in Section 13.b. of the Agreement based upon Respondents' failure to fulfill the development schedule, which Claimants did on October 15, 2002;

3. As a result of Respondents' development schedule default and Claimants' exercise of their Section 13.b. remedy, Respondents lost the right, power, and License (i) to use the Trademarks in connection with any Clubs which were not, as of October 15, 2002, under construction or open for business and operated by Respondents, an Affiliate of Respondents, or other Operator and (ii) to sub-license Third Parties to use the Trademarks in connection with any new Clubs, and these rights reverted to Claimants;

4. As a result of Respondents' development schedule default and Claimants' exercise of their Section 13.b. remedy, Claimants are (and, from the

date the remedy was exercised, have been) entitled to open and/or license new Clubs in the Territory; provided, however, that as noted in the September 7, 2004, Order re Motions for Summary Adjudication, this Award does not decide whether Claimant would violate the covenant of good faith and fair dealing by opening a Club in a metropolitan area where Respondents presently operate a Club;

5. Section 9.j. of the Agreement is a valid and enforceable in-term covenant not to compete and shall remain valid and enforceable within the United States for the remaining Term of the Agreement;

6. Respondents and their Affiliates are enjoined for the remaining Term of the Agreement from owning or operating any bar, restaurant, nightclub, or other facility which presents live stand-up or sketch comedy performances or live improvisational performances, other than (i) the Melrose Improv and Second City, (ii) existing Clubs operated by Respondents, an Affiliate of Respondents, other Operator that were under construction or open for business as of October 15, 2002, and (iii) any additional Clubs as Claimants may authorize Respondents or their Affiliates to open or other Clubs licensed by Claimants in which Respondents or their Affiliates have acquired or may acquire an interest;

7. Respondents and their Affiliates are enjoined for the remaining Term of the Agreement from changing the name of any of their existing Clubs and continuing to operate any such club as a bar, restaurant, nightclub or other facility which

presents live stand-up or sketch comedy performances or live improvisational performances, and so long as those Clubs are open, Respondents shall pay Claimants the fees and royalties provided in the Agreement;

8. Claimants are entitled to retain the non-refundable advances made by Respondents pursuant to Sections 6.b. and 12.b. of the Agreement with respect to periods through June 2002;

9. Respondents shall recover from Claimants the sum of $50,000, reflecting the total amount of advances made by Respondents pursuant to Section 6.b. and 12.b. of the Agreement with respect to periods after June 2002. Claimants may, at their election, credit such amount against my amounts due from Respondents to Claimants, including but not limited to the amount due pursuant to paragraph 10 hereof, or pay such amounts to Respondents; and

10. Claimants are the prevailing parties in this Arbitration and the related District Court action to compel arbitration, except with respect to the separate and independent counterclaim as to booking fees in paragraphs 5-7 of Respondents' Second Amended Counterclaim, which remains pending. Pursuant to Section 22 of the Agreement, Respondents shall pay to Claimants the reasonable attorneys' fees in the amount of $362,767.16 and costs in the amount of $16,261.96 that Claimants have incurred in this Arbitration and in the District Court action.

In light of the relief sought, the Arbitrator has found it unnecessary to decide Claimants' other claims of breach, and neither the Arbitrators' Orders nor this Award shall have any preclusive effect as to those claims. Respondents' counterclaims (except with respect to the separate and independent counterclaim as to booking fees in paragraphs 5-7 of Respondents' Second Amended Counterclaim, which remains pending before the Arbitrator) are denied.

This Award is a final determination of the claims and counterclaims submitted for arbitration in the Amended Demand for Arbitration dated April 6, 2004, the more specific statement of claims asserted and relief sought dated June 15, 2004, and the Amended Answering Statement and Counterclaim dated June 25, 2004, and also of the counterclaim as to license fees set forth in paragraphs 1 through 4 of Respondents' Second Amended Counterclaim dated November 8, 2004. This Award does not decide Respondents' booking fee claim alleged in paragraphs 5-7 of the Second Amended Counterclaim, which remains pending. That claim is factually and legally separate from the claims determined by this Award. The Arbitrator believes that it would be in the interest of justice for this Award to be confirmable without further delay and intends this Award to be subject to immediate confirmation in any court of competent jurisdiction notwithstanding the pendency of a separate and independent claim before the Arbitrator.

The Arbitrator has retained jurisdiction to determine the booking fee claim alleged in the Second Amended Counterclaim and to allocate

among the parties the administrative fees of the American Arbitration Association and the fees of the Arbitrator.

Dated: February 25, 2005 /s/ Richard R. Mainland
Arbitrator

Appendix H

American Arbitration Association

Case No.: 72 181 00274 04 NADE

IMPROV WEST ASSOCIATES and CALIFORNIA COMEDY, INC.,

Claimants,

v.

COMEDY CLUB, INC. and AL COPELAND INVESTMENTS, INC.,

Respondents.

Oct. 22. 2004

OPINION

Respondents Comedy Club, Inc. and Al Copeland Investment, Inc. (collectively "Respondent") have moved for reconsideration of the arbitrator's summary adjudication order. Claimants Improv West Associates and California Comedy, Inc. (collectively "Claimant") oppose the motion for reconsideration and have filed a supplemental motion for summary adjudication.

The arbitrator has read and considered the motions, the memoranda, the separate statements of undisputed facts and exhibits filed therewith, and

has considered the arguments of counsel at a hearing on October 22, 2004. The motions having been submitted for decision, the arbitrator denies the motion for reconsideration and grants the supplemental motion for summary adjudication. The arbitrator's reasons are briefly summarized below.

I. RESPONDENT'S MOTION FOR RECONSIDERATION OF SUMMARY ADJUDICATION ORDER

This motion amplifies an argument made in Respondent's reply memorandum (pp. 17- 20), which the arbitrator considered in making his summary adjudication ruling. The present motion is not a motion for reconsideration in the usual sense – no new law or newly discovered facts are cited. However, arbitration procedures are more flexible than court litigation and the motion will be considered on the merits.

Decisions assessing covenants not to compete under California Business & Professions Code §16600 consider whether the contract imposes total or partial restraints. *Campbell v. Board of Trustees*, 817 F. 2d 499 (9th Cir. 1987). However, unlike some other states, California does not apply a "reasonableness" test in assessing the validity of a contractual restriction under §16600. *Campbell, supra* at 502; *Commercial Packaging. Inc. v. TIPS Package Engineering. Inc.*, 126 F. 3d 1131, 1133 (9th Cir. 1997).

As determined in the summary adjudication

order, the covenant not to compete in paragraph 9j of the Trademark License Agreement is a partial restraint on Respondent's ability to engage in the comedy club business. Indeed, the Agreement provides a framework for Respondent to engage in the comedy club business during the term of the Agreement, but only as a licensee of Claimant.

Respondent argues that the covenant not to compete in paragraph 9j of the Trademark License Agreement will unreasonably impact Respondent, because of the limited number of clubs Respondent currently operates, the uncertain financial status of these clubs and Respondents' loss of its right to license additional clubs under the Agreement. This type of "unreasonableness" argument is not available under California law. *Id.* Moreover, Respondent's loss of the right to license new IMPROV clubs results from its own breach of the Agreement by failing to meet the development schedule, and Respondent should not be allowed to use its own default to invalidate an otherwise valid partial restraint on competition.

Dayton Time Lock Service, Inc. v. The Silent Watchman Corp., 52 Cal. App. 3d 1 (1975), relied on by Respondent, is inapplicable. That case involved an attack on an exclusive dealing contract under the antitrust laws. The cases cited in the portion of the Dayton opinion relied on by Respondent involved validity of exclusive dealing contracts under the federal Sherman Act. The type of "rule of reason" analysis applied in antitrust cases - involving the determination whether a particular agreement unreasonably restricts competition generally in a

defined geographic and product market - is not applicable to a determination of illegality under Section 16600. California's antitrust statute, the Cartwright Act, is separate and distinct from §16600 of the Business & Professions Code. See B&P Code, §16700, *et seq.*

Accordingly, the motion for reconsideration is denied.

II. CLAIMANT'S SUPPLEMENTAL MOTION FOR SUMMARY ADJUDICATION

This motion seeks a ruling that a breach by Claimant of paragraph 10 of the October 19, 1999 Amendment to Trademark License Agreement does not excuse Respondent's obligation to meet the development schedule for new clubs contained in paragraph 1 of the Amendment

The motion raises the issue whether the covenant in paragraph 10 is also a condition to Respondent's obligation to comply with the development schedule in paragraph 1. If paragraph 10 is a only a covenant, a breach by Claimant would give rise to a claim for damages, but would not excuse Respondent from its obligation to perform under paragraph 1. If, on the other hand, paragraph 10 is also a condition a breach would excuse Respondent's obligation to perform. Witkin, *Summary of California Law.* Contracts, §723; Williston on Contracts, §38.5. Determining whether a contractual covenant is also a condition is a matter of interpreting the contract language to determine the parties' intent.

Respondent concedes that performance of the paragraph 10 covenant was not a condition precedent to its development schedule obligation, but argues that the two covenants were concurrent conditions, relying on a "presumption" that covenants in a bilateral contract which to be performed during the same general time period should be presumed to be conditions concurrent. The arbitrator does not read the authorities cited by the parties as establishing such a sweeping presumption. The "concurrent conditions" cases cited by Respondent involve transactions for the sale of property or situations in which the parties were to exchange consideration (e.g., a deed and a purchase price) at the same time. *See Ninety Nine Investment, Ltd v. Oversas Courier Service*, 113 Cal. App. 4th 1118 (2003); *Rubin v. Fuchs*, 1 Cal. 3d 50 (1969). Respondent also cites cases where there was a clear failure of consideration owed by one party, *Pry Corporation of American v. Leach*, 177 Cal. App. 2d 632 (I960), or where the parties agreement clearly intended a condition to exist. *Wiz Technology, Inc. v. Coopers Lybrand LLP*, 106 Cal. App. 4th 1 (2003). The arbitrator believes that these cases are factually distinguishable from the present case.

Here, the Amendment does not contain language indicating that performance of the obligation in paragraph 10 was intended to be a condition to Respondent's development schedule obligation (although the absence of such express language is not determinative of the issue). In paragraph 10 Claimant agrees only to use its "best efforts" to "clear up" unspecified issues relating to Claimant's "franchise deals." No time is specified for

using these "best efforts." There is no definitive commitment that the "issues" will in fact be "cleared up." The development schedule provision in paragraph 1, by contrast, is highly specific in the number and time of opening new clubs over a period of several years.

The paragraph 10 covenant is not directly linked to Respondent's development of new clubs, but rather concerns Claimant's dealings with other licensees in geographical areas outside Respondent's territory. In view of the contractual language and the nature of these two quite different covenants, the most reasonable interpretation is that a breach of paragraph 10 gives rise to a damages claim but does not excuse Respondents' failure to meet the development schedule. *See, e.g., Starr v. Davis*, 105 Cal. App. 632 (1930) (breach of covenant not to compete by seller of a business did not excuse buyer's duty to pay purchase price); *Consumer Action v. Wells Fargo Bank*, 2002 WL 818256 ("... where the promises are to be performed at different times, they are generally deemed independent covenants and not concurrent conditions"); *Kaupke y. Lemoore Canal and Irrigation Co.*, 20 Cal. App. 2d 554, 557 (1937); Witkin, *supra*, §754.

For these reasons the supplemental motion for summary adjudication is granted. This ruling is based on the factual record developed in the original cross-motions for summary adjudication filed by the parties and in connection with Claimant's supplemental motion for summary adjudication. These motions followed document production

conducted by the parties relating to the summary adjudication issues. Good cause has not been shown for any further expansion of the factual record in connection with the motion.

Because the issue can be resolved as a matter of contractual interpretation, it is not necessary to reach or decide the separate issue of whether Respondents' alleged failure to make a payment to Claimant resulted in a loss of exclusivity of the license or gave Claimant the right to open or license new clubs in the Territory.

Dated: October 22, 2004

Richard R. Mainland
Arbitrator

Appendix I

American Arbitration Association

Case No.: 72 181 00274 04 NADE

IMPROV WEST ASSOCIATES and CALIFORNIA COMEDY, INC.,

Claimants,

v.

COMEDY CLUB, INC. and AL COPELAND INVESTMENTS, INC.,

Respondents.

Sept. 7, 2004

ORDER RE MOTIONS FOR SUMMARY ADJUDICATION

Claimants Improv West Associate and California Comedy, Inc. (collectively "Claimant") has moved for summary adjudication in this arbitration. Respondents Comedy Club, Inc. and Al Copeland Investment, Inc. (collectively "Respondent") opposes Claimant's motion and has cross-moved for summary adjudication.

The arbitrator has read and considered the motions, the memoranda, the separate statements of undisputed facts and exhibits filed therewith, and

has considered the arguments of counsel at the hearing on August 10, 2004. The motions having been submitted for decision, the arbitrator grants the summary adjudication motion of Claimant, and denies the motion for summary adjudication of Respondent, on the terms end conditions set forth hereinbelow.

I. THE APPLICABLE LEGAL STANDARDS

The June 13, 1999 Trademark License Agreement, as amended (the "Agreement") contains an arbitration clause and a clause selecting California law. Claimant's Motion, Ex. A, ¶¶17 and 22. Under California law, orders equivalent to summary judgment or summary adjudication of issues may be rendered in arbitration based on documentary evidence and without live testimony. *Schlessinger v. Rosenfeld, Meyer & Susman*, 40 Cal, App. 4th 1096 (1995). The parties and the arbitrator are not bound to follow the specific rules, procedures and technical requirements contained in Section 437c of the Code of Civil Procedure, California's summary judgment statute. *Id.* at 1104. However, the basic purpose of summary adjudication in arbitration is the same as in court proceedings—to decide issues as a matter of law where there is no genuine dispute as to the facts.

II. FACTUAL BACKGROUND

Claimant has for many years operated comedy nightclubs under the "IMPROV" name and has licensed others to operate comedy clubs using that name. Claimant's flagship club was the IMPROV

club on Melrose Avenue in Los Angeles.

In 1998 Al Copeland, a New Orleans, Louisiana restaurateur, negotiated with Claimant for a transaction that would expand the IMPROV franchise nationwide. These negotiations culminated in the Agreement, as well as an agreement for sale of the Melrose club to Respondent.

The Agreement granted to Respondent "the exclusive right, power and license" to use the IMPROV trademarks in comedy clubs nationwide, except for areas covered by Claimant's existing licenses and certain areas in Nevada and Mississippi (the "Territory"). The Agreement was for a 20-year term through May 31, 2019, with an option by Respondent to renew for an additional 10 years through 2029.

Paragraph 12 of the Agreement sets forth a development schedule for the opening of a minimum number of new clubs by Respondents during the early years of the contract term. Under an amendment effective October 19, 1999, Respondent agreed to open 4 clubs in each of the 3 years ending October 31, 2001, 2002 and 2003, respectively, for a total of 12 clubs by October 31, 2003 (the "development schedule"). Claimant's Ex. B, ¶1.

The parties agree that Respondent did not meet the development schedule. Claimant's Statement of Undisputed Facts ("CSUF"), ¶4; Respondent's Response to Claimant Statement of

Undisputed Facts, ¶4.[1]

Paragraph 13.b of the Agreement provides the following "sole remedy" for a failure to fulfill the development schedule:

> Upon notice to Licensee. Licensee shall lose the right, power and License (i) to use (he [IMPROV] Trademarks in connection with any Clubs which are not, as of the date of such failure, under construction or open for business and operated by Licensee, an Affiliate of Licensee or other Operator and (ii) to sub-license Third Parties use the [IMPROV marks] in connection with any new Clubs.

On October 15, 2002, Claimant gave written notice of its intent to declare an "Event of Default" under Paragraph 13.b of the Agreement, including termination of Respondents right, power and license to use the IMPROV marks in connection with any

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[1] The parties' versions of how many Clubs Respondent opened and by what dates is somewhat conflicting. Claimant's Motion states that by October 13, 2002, Respondent had opened three Clubs, falling five short of the required number, and that Respondent is part owner of three other Clubs along with Claimant's long-time licensee. Claimant's Motion at p. 5. Respondent states that by October 2002. It was "operating or franchising 6 Clubs." Cross-Motion at p. 8. It is unclear whether Respondent contends that these 6 Clubs qualify for purposes of the development schedule. However, in view of the parties' agreement that the development schedule was not met, the Motions may be decided without determining the precise number of qualifying Clubs opened by Respondent by the applicable deadlines.

Clubs which were not, as of October 13, 2002, under construction or open for business. CSUF, Ex. C.

By late 2003 various disputes had arisen under the Agreement. Most significantly, Claimant contended that Respondent had lost its exclusivity rights under the Agreement and that Claimant was free to develop Clubs in Respondent's territory, either on its own or through licensees. Respondent maintained, to the contrary, that it retained these exclusivity rights, precluding Claimant from opening Clubs in the territory. In addition, a dispute had arisen regarding paragraph 9.j of the Agreement which provides:

> "Licensee shall not own or operate, and Licensee shall ensure that none of its Affiliates shall own or operate any bar, restaurant, nightclub or other facility which presents live stand-up or sketch comedy performances or live improvisational performances, other than the Melrose Improv or a Club, or Second City."

Claimant contended that this covenant not to compete prevented Respondent from opening Clubs in the territory under non-IMPROV trade names, while Respondent contended that this covenant was unenforceable under Section 16600 of the California Business & Professions Code.

On November 7, 2003, Respondent filed a declaratory relief action in the federal court in Los Angeles. *Comedy Club, Inc., et al., v. Improv West*

Associates, et al., U.S. Dist. Ct., C. D. Cal., Case No. CV-03-8134 WMB. On March 5, 2004, Claimant demanded arbitration of the parties' disputes. Thereafter, the District Court granted Claimant's motion to compel arbitration of the claims alleged in the federal action. Respondent thereupon asserted its claims against Claimants by a Counterclaim In this arbitration.

III. THE PARTIES MOTIONS FOR SUMMARY ADJUDICATION

A. The Legal Consequences of Respondent's Failure to Meet the Development Schedule.

Claimant contends that upon Respondent's failure to meet the development schedule Claimant was entitled to open new Improv clubs in the previously licensed Territory and to license others to open such clubs, i.e., to continue the national development of the IMPROV brand. Respondent argues, to the contrary, that even if it lost the right to open or sub-license new clubs, it retained the exclusive rights to the IMPROV trademarks in the Territory, thereby precluding Claimant and its licensees from doing so. Respondent has cross-moved for summary adjudication on this issue and also has moved for summary adjudication that Claimant breached the Agreement by licensing the IMPROV marks for a Houston area club. Respondent's Cross-Motion, p. 14. This dispute is resolvable on summary adjudication, because it is one of contractual interpretation and is not the

subject of factual disputes.[2]

Under California Law, contracts should be interpreted to carry out the expressed intentions of the parties. Cal. Civ. Code, §1636. Where the contract language is clear and explicit and does not lead to absurd results, the analysis need go no further. *Shaw v. Repents of the University of California*, 58 Cal. App. 4th 44, 53 (1997). However, this rule is qualified by other principles of contractual interpretation. For example, the words of a contract may be explained by reference to the circumstances under which the contract was made. (Civ. Code §1647.) And literal language of a contract does not control if it leads to absurdity or if it is wholly inconsistent with the main intention of the parties (Civ. Code, §§1638, 1653).

Construing the Agreement in light of these principles, the arbitrator finds that upon Respondent's failure to fulfill the development schedule Respondent lost the right to open new IMPROV clubs and lost the exclusivity of its license, i.e., Claimant became entitled to operate and license IMPROV clubs in the Territory. The arbitrator bases this conclusion on his interpretation of the language of the Agreement and upon the surrounding circumstances and purposes of the Agreement as evidenced by that language. The text

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[2] Respondent does contend that, assuming Claimant's construction of the Agreement is accepted, there it a factual issue concerning whether its development schedule default was excused by Claimant's alleged breaches of the Agreement, as amended. This argument is discussed in Part III(C) below.

of the Agreement grants to Respondent the "exclusive right, power and license" to use the IMPROV marks in connection with comedy clubs. (¶2.a). The arbitrator finds that the words "exclusive" modifies "right, power and license." Paragraph 13-b provides that upon Respondent's failure to meet the development schedule, it would "lose" that "right, power and license," in connection with new clubs. (¶13.b).[3] All rights not licensed to Respondent are reserved to Claimant (¶3.d). Therefore, upon Respondent's "loss" of the right to open new IMPROV clubs, that right reverted to Claimant

Because Respondent lost its exclusive license in the Territory, the words "sole remedy" in paragraph 13.b do not preclude Claimant from opening IMPROV clubs in the Territory. The right of Claimant to do so flows from Respondent's loss of its exclusive license. Respondent correctly points out that various detailed remedies are spelled out for "curable" defaults in paragraph 13.a of the Agreement, including an express provision in paragraph 13.a(3) allowing Claimant to "change the license from an exclusive to a non-exclusive license" and to open clubs in the Territory. However, in the arbitrator's view the fact that this remedy is spelled out in a detailed list of alternative remedies in paragraph 13.a does not warrant the restrictive interpretation of paragraph 13.b contended for by

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[3] The arbitrator does not accept Respondent's argument that capitalization of the word "License" in paragraph 13.b creates a "redundancy" requiring the arbitrator to accept Respondent's interpretation concerning loss of exclusivity.

Respondent, particularly in light of the purpose of the development schedule itself discussed below.

The Territory exclusively licensed to Respondent was large, comprising the 48 states less Nevada, a part of Mississippi, and several metropolitan areas previously licensed to other parties.

The purpose of the development schedule was to give Claimant the assurance that there would be sufficient expansion of the IMPROV franchise early in the contract terms to warrant the grant of such expansive and exclusive rights to Respondent. It is unreasonable to construe the Agreement to provide that Respondent could fail to meet the development schedule *and* retain its exclusive rights to the entire Territory. Under Respondent's interpretation of paragraph 13.d, its failure to develop clubs in the Territory would leave Claimant powerless to seek alternative ways of doing so. Such an interpretation appears directly contrary to the purpose of the development schedule requirement itself.

Respondent contends that retaining its exclusive rights throughout the Territory for the contract term would not necessarily "freeze" IMPROV development, because failure to meet the development schedule "simply shifts discretion to the Claimants as to whether they wish to halt further brand development altogether, or to waive the default and allow development to go forth at a slower pace." Cross-Motion at p. 19. This argument fails to recognize another equally probable scenario: that Respondent chooses to cease further development of

the IMPROV brand altogether, leaving Claimant (under Respondent's construction of the contract) with development frozen at an inadequate level for up to 20 years. Moreover, even with the loss of Respondents' exclusivity; development can also go forward "at a slower pace" if it is in the parties' mutual interests to do so. Claimant and Respondent are free to negotiate for new locations to be opened by Respondent. In the Territory, notwithstanding its loss of contractual exclusivity in the Territory.

Because the arbitrator construes paragraphs 12.a and 13.b to provide for Respondent's loss of exclusivity upon a failure to meet the development schedule, Claimant's Motion is granted and Respondent's Cross-Motion on this issue is denied. It also follows that Claimant was within its rights in licensing a Club in the Houston area, and Respondent's cross-motion alleging a breach from such licensing is denied.[4]

B. The Covenant Not to Compete.

Section 16600 of the California Business & Professions Code provides that "[e]xcept as provided in this chapter, every contract by which anyone is restrained from engaging in a lawful profession,

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[4] In ruling that Respondent's development schedule breach resulted in a loss of Respondent's exclusive license in the Territory, the arbitrator does not decide, and expresses no opinion on, whether Claimant would violate the covenant of good faith and fair dealing by opening a Club in a metropolitan area where Respondent presently operates a Club. *See In re Vylene Enterprises. Inc., v. Naugles, Inc.*, 90 F. 3d 1472 (9th Cir. 1996).

trade or business of any kind is to that extent void." This provision is "an expression of public policy to ensure that every citizen shall retain the right to pursue any lawful employment and enterprise of their choice." *Metro Traffic Control, Inc. v. Shadow Traffic Network*, 22 Cal. App, 4th 853, 859 (1994). Although the language of Section 16600 is broad in scope, court decisions have upheld agreements limiting competition in a variety of contexts. For example, it has been, held that Section 16600 applies only to covenants preventing one from engaging in an entire business, trade or profession." *Campbell v. Board of Trustees of Stanford University*, 817 F. 2d 499, 502 (9th Cir. 1987). And covenants not to compete *during the term* of an employment agreement or distribution contract are regularly upheld. *Shaklee U.S., Inc. v. Giddens*, 1991 U.S. App. LEXIS 11617, *8-9 (9th Cir. 1991).

Respondent's principal argument is that Paragraph 9.j of the Agreement prohibits competition to the comedy club business *forever*, and thus cannot be upheld as an "in-term" covenant not to compete. The arbitrator disagrees. Paragraph 9.J is silent on the duration of the covenant. However, Section 3.a of the Agreement provides:

"Upon termination of this Agreement, the License and the rights granted hereunder and the obligations imposed hereunder shall cease, except that Licensee and any sub-licensee shall remain liable for any obligations remaining hereunder including obligations accrued as of the date of such termination and except as otherwise expressly set forth herein."

Nowhere in the Agreement is it "expressly set forth" that the covenant in paragraph 9.j extends beyond the termination of the Agreement. To overcome paragraph 3.d, Respondent points to the "survival clause" in paragraph 15 of the Agreement, - which provides:

"All representations, warranties, covenants and agreements made by Licensor or Licensee in this Agreement or the Asset Purchase Agreement shall survive the termination of this Agreement, including the agreements to indemnify any party, and shall, except to the extent specifically limited elsewhere in this Agreement, be perpetual in term. The various provisions of this Agreement shall be severable, and the non-enforceability of one shall not affect the enforceability of the others."

Similar clauses have been interpreted to mean that the time to sue for breach of contractual covenants extends beyond the specified date—here the termination of the Agreement—not that the covenant themselves continue in existence beyond that date. *Herring v. Teledyne*, 256 F. Supp. 2d 1118 (S.D. Cal. 2002). Where, as here, the contract does not specify a time period for bringing suit the statutes of limitations under applicable law apply and run from the time of the breach. *Id.*, at 1133. As so interpreted, there is no conflict between paragraphs 3.1 and 15 of the Agreement

There ere other reasons why the covenant not to compete in paragraph 9.j. should not be interpreted to extend beyond the Agreement's term. To the extent the language of paragraphs 3.d and 15

are in conflict,[5] the arbitrator will construe the Agreement in a sensible way to carry out the parties' purpose and intent. As Claimant points out, It would make no sense to construe the agreement to extend indefinitely the covenants which apply only to operations during the term of the Agreement, such as covenants to provide financial information. The language of paragraph 3.d., contemplating termination of the parties' covenants upon termination of the Agreement "except as otherwise expressly set forth herein" is a more rational provision than one extending all contractual covenants forever. Respondent apparently agrees that the Agreement does not provide that all covenants extend indefinitely, but asks the arbitrator to conclude that the covenant in paragraph 9.j does extend Indefinitely. Respondent's Reply Memorandum, p. 13. However, there is no reason to resolve any ambiguity or conflict in contractual language by an interpretation that would render it unlawful. To the contrary, under California, law a contract should "receive such an Interpretation as will make it lawful, operative, definite, reasonable, and capable of being carried into effect, if it can be done without violating the intention of the parties." Cal. Civ. Code §§1643, 3541. The arbitrator construes paragraph 9.j as an in-term covenant not to compete, which expires upon termination of the Agreement.

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[5] If such a conflict existed it would not be the only conflicting language in the Agreement. In its order compelling arbitration the District Court noted that the dispute resolution provisions of the Agreement were "internally inconsistent." See Order Sending Parties to Arbitration, filed July 30, 2004.

The authorities cited by the parties support the enforceability of in-term covenants not to compete. Such covenants have been held enforceable during the terms of employments agreements, *Fowler v. Varian Assoc's Inc.*, 196 Cal. App. 3d 34, 44 (1987), supplier-distributor agreements, *Shaklee U.S., Inc. v. Giddens*, 1991 U.S. App. LEXIS 11617 (9th Cir. 1991), and franchise agreements. *Keating v. Baskin-Robbins, USA, Co.*, 2001 WL 407017 (E.D.N.C.) (applying California law) and *Great Frame-Up Systems, Inc. v. Jazayeri Enterprises, Inc.*, 789 F. Supp. 253 (E.D. Ill. 1992) (applying California law). Although the reasoning in these decisions is sparse, they do emphasize that in-term restrictions are only "partial" restraints on competition, because the restrained party (whether employee, distributor or franchisee) may continue to engage in the relevant business during the term of his or her agreement with the employer, supplier or franchisor. Respondent has not cited any decision invalidating in-term covenants not to compete under Section 16600.[6] The arbitrator finds, therefore, that paragraph 9.j of the Agreement is a valid and enforceable in-term covenant under California law.

Alternatively, even if the paragraph 9.j covenant could be construed to extend beyond the contract term, it is enforceable up to the end of the

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[6] Respondent has cited authorities striking down covenants not to compete in franchise or similar agreements *after* expiration of the contract term, but such decisions are inapplicable to paragraph 9.j as construed herein. *E.g., Scott v. Snelling and Snelling*, 732 F. Supp, 1034, 1042 (N.D. Cal. 1990); *Latona v. Aetna U.S. Healthcare, Inc.*, 82 F. Supp, 2d 1089, 1094 (CD, Cal. 1999).

contract term under California's "rule of severability," allowing enforcement of overbroad covenants up to their lawful temporal and geographical limits, *Swenson v. File.*, 3 Cal. 3d 389, 395 (1970); *Hill Medical Corp. v. Wycoff*, 86 Cal. App. 4th 895, 908 (2001). These decisions are more applicable to the present fact situation than *Kolani v. Gluska*, 64 Cal. App. 4th 402, 407-08 (1998), relied on by Respondent, which declined to convert an invalid covenant not to compete into valid trade secret protection clause. *Latona v. Aetna U.S. Healthcare, Inc.*, is also distinguishable. *Latona* held that an employer violated California public policy by firing an employee who refused to sign a covenant not to compete that violated Section 16600. The covenant prohibited all competition by the employee for six months after termination of employment, and thus clearly violated Section 16600. The Court held that the employer could not excuse its conduct by asking the Court to "reform" the contract to make it valid, either by excising the post-employment restraint or by converting it into a trade secret protection clause. The Court noted the *in terrorem* of allowing employers who require employees to sign Invalid covenants to use the Courts to reform such agreements when challenged. Such fact situations arc far removed from the present case, where the covenant does not expressly extend beyond the contract term and the parties are equally sophisticated and alert to their legal rights.

Respondent contends that the paragraph 9.j covenant is overly broad geographically and is unenforceable for that separate reason. To the extent the covenant covers the United States the

arbitrator finds that it is geographically reasonable and enforceable. The exclusive Territory granted to Respondent by the original license—the territory the parties anticipated developing through Respondent activities-covered most of the United States, except for the areas already licensed by Claimant to other parties and the State of Nevada and a limited area in Mississippi which were reserved for separate development by Claimant. It is therefore not unreasonable to enforce the covenant in these same areas--the United States. The arbitrator expresses no opinion and does not decide whether the covenant is enforceable outside the United States.

C, Issues Not Summarily Adjudicated

It is the intent of this order to summarily adjudicate (i) (he legal consequences flowing under the Agreement from Respondent's failure to meet the development schedule and (ii) the enforceability of the covenant not to compete in paragraph 9j of the Agreement. There are a number of other claims and/or defenses mentioned in the parties' summary adjudication briefs that are not adjudicated by this order.

Respondent contends that even if Claimant's interpretation of the Agreement regarding loss of exclusivity is accepted, Claimant's motion must be denied because there are "factual disputes" as to whether Respondent's development schedule default was excused. Cross-Motion at p. 30. Specifically, Respondent contends that its "failure to adhere to the development schedule was caused in part by Claimants' own failure to police its pre-existing

licensees, and to exercise its contractual lights against them to bring them up to the quality standard set by Respondents." Cross-Motion at p. 30. This conduct, says Respondent, breached paragraph 10 of the October 19, 1999, amendment to the Agreement, which provides that "Improv West will provide its best efforts to clear up any and all issues related to its franchise deals." CSUF, Ex. B.

Respondent has also moved for summary adjudication in its favor respecting! Claimant's allegations of other breaches of the Agreement by Respondent. Cross-Motion, pp. 22-28. These alleged breaches include failure to provide certain financial information, failure to make certain payments, anticipatory breach of the Agreement by leasing a site for an Atlanta club after loss of Respondent's right to open new clubs, and breach of the Agreement's arbitration clause by bringing the related federal action. Claimant did not move for summary adjudication on these separate alleged breaches.

These claims and defenses are not ripe for summary adjudication at this time. The parties' papers contain assertions of fact and arguments on these matters, and certain correspondence has been submitted that may have some bearing on them. However, the *evidence* before the arbitrator is inadequate to provide a sufficient basis for summary adjudication for or against either party on these issues. Although summary adjudication in arbitration need not follow the specific procedures under the California's summary judgment statute (C.C.P. §437c). It is essential, in the arbitrator's

view, that summary adjudication in arbitration be based on facts established either by admissions of the parries or by uncontroverted competent evidence. No testimony of witnesses has been submitted, and even if the arbitrator considers all of the correspondence and other documents supplied in connection with these motions, the adjudication on these fact-intensive matters cannot be done summarily.[7]

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[7] The arbitrator specifically notes that he is not deciding at this time (i) what obligations, if any, were imposed on Claimant by paragraph 10 of the amendment to the Agreement (ii) whether, as a matter of law, a breach by Claimant of paragraph 10 would excuse Respondent's development schedule default, or (iii) whether Respondent must show that any alleged breach of paragraph 10 by Claimant caused Respondents' failure to meet the development schedule in order to excuse Respondent's development schedule default.

This order is without prejudice to either party moving for summary adjudication on any or all of these additional tones, which motions must be supported by competent evidence. Absent any such motions, these claims and defenses will be determined after the evidentiary hearing.

Dated: Sept. 7, 2004

Richard R. Mainland
Arbitrator

Appendix J

United States Court of Appeals, Ninth Circuit

NOS. 05-55739, 05-56100

COMEDY CLUB, INC., a Louisiana corporation; Al Copeland Investments, Inc., a Louisiana corporation,

Plaintiffs-Appellants,

v.

IMPROV WEST ASSOCIATES, a California Limited Partnership; California Comedy, Inc., a California corporation,

Defendants-Appellees.

Comedy Club, Inc., a Louisiana corporation; Al Copeland Investments, Inc., a Louisiana corporation,

Plaintiffs-Appellants,

v.

Improv West Associates, a California Limited Partnership; California Comedy, Inc., a California corporation,

Defendants-Appellees.

Jan. 23, 2008

ORDER ON PETITION FOR REHEARING AND REHEARING EN BANC

Before: JEROME FARRIS and RONALD M. GOULD, Circuit Judges, and KEVIN THOMAS DUFFY,* District Judge.

The opinion filed on September 7, 2007 and published at 502 F.3d 1100 is AMENDED as follows.

The final parenthetical in the first full paragraph on page 1114 states:

> (reasoning that a contract can not place "a substantial segment of the market off limits").

> The final parenthetical in the first full paragraph on page 1114 is deleted in its entirety and replaced with the following:(reasoning that a contract cannot place "a substantial segment of the market off limits").

> The second sentence in footnote 17 on page 1114 states: However, *Dayton Time Lock* made clear that it was assessing the requirements of CBPC §16600, and its plain language applied standards from antitrust cases in aid of its application of §16600, which was an issue under review.

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* The Honorable Kevin Thomas Duffy, Senior United States District Judge for the Southern District of New York, sitting by designation.

The second sentence in footnote 17 on page 1114 is deleted in its entirety and replaced with the following: However, *Dayton Time Lock* made clear that it was assessing the requirements of CBPC §16600, and its plain language applied standards from antitrust cases in aid of its application of §16600.

The panel, as constituted above, has unanimously voted to deny the petition for panel rehearing. Judge Gould voted to deny the petition for rehearing en banc, and Judges Farris and Duffy have so recommended.

The petition for en banc rehearing has been circulated to the full court, and no judge has requested a vote on whether to rehear the matter en banc. Fed. R.App. P. 35(b).

The petition for panel rehearing and the petition for rehearing en banc are denied. No further petitions for rehearing or rehearing en banc will be accepted.

IT IS SO ORDERED.

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(2)

Supreme Court, U.S.
FILED
JUN 23 2008
OFFICE OF THE CLERK

No. 07-1334

IN THE

Supreme Court of the United States

IMPROV WEST ASSOCIATES, and
CALIFORNIA COMEDY, INC.,

Petitioners,

v.

COMEDY CLUB, INC. and
AL COPELAND INVESTMENTS, INC.,

Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE
UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

BRIEF IN OPPOSITION

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COUNTERSTATEMENT OF QUESTIONS PRESENTED[1]

1. Should the Court grant certiorari when the Ninth Circuit partially reversed an arbitrator's decision that was in "manifest disregard of the law", a standard this Court has found to be consistent with the parameters of the Federal Arbitration Act?

2. Should the Court grant certiorari when this Court, the Ninth Circuit and every other circuit in the nation applies the "manifest disregard of law" standard to reviewing arbitral decisions?

3. Should the Court grant certiorari merely because the Ninth Circuit allegedly misapplied an otherwise established and correctly stated rule of law?

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[1] Petitioners are not seeking re-hearing on the Ninth Circuit's determination that the arbitrator exceeded the scope of his authority in extending the application of the parties' contract to all "affiliates". Accordingly, Respondents do not revisit that issue either.

CORPORATE DISCLOSURE STATEMENT

The Respondents, Comedy Club, Inc. and Al Copeland Investments, Inc. have no parent corporation, and no publicly held company owns 10% or more of their stock.

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SUMMARY

Petitioners here seek review of the Ninth Circuit's ruling below finding that an arbitrator who was aware of a material state law but chose to ignore it acted in "manifest disregard of the law." As conceded by Petitioners in their Ninth Circuit briefs, "manifest disregard of the law" is a historically grounded and well-established legal standard for reversing an arbitral decision. As many courts have iterated, it is a notably high standard arising out of and generally defining the specific enumerated grounds set forth in the Federal Arbitration Act (FAA). There are no new issues of law here and the governing legal framework has been clearly set forth in this Court's prior decisions.

The decision below establishes no new principles, but merely applies this Court's well-established rule. Petitioners argue that the Ninth Circuit below misapplied this well-established law and in doing so is squarely at odds with every other circuit in the country. This is simply not accurate – the Ninth Circuit properly applied the law in a manner consistent with this Court's precedent and with other circuits. Moreover, the circuits themselves consistently apply the "manifest disregard of the law" standard and there is no split between the federal courts on the issue.

Finally, Petitioner's invocation of this Court's recent decision in *Hall Street Associates, LLC v. Mattel, Inc.* is a hook without a point. That holding does not apply here because it solely raised (and answered in the negative) the question of whether parties to an arbitration agreement could contractually add grounds

for reversal of an arbitral decision when those grounds are not included in the FAA. This is inapposite here because no such issue arose in this case. The parties here did not attempt to contract around the FAA nor did the Ninth Circuit below address the issue whatsoever. Moreover, although not the main issue in that case, *Hall Street* expressly acknowledged that "the manifest disregard of the law" standard arose out this Court's own precedent and is believed to be a summary articulation of the grounds for reversal set forth in the FAA. In accordance with that precedent, and its own, the Ninth Circuit below applied the well-established standard of "manifest disregard of the law" to the arbitration decision before it and found that the arbitrator indeed manifestly disregarded the law. This finding was amply supported by the record.[2]

Because the there is no mature conflict in the courts of appeals and because the Ninth Circuit's ruling below is consistent with *Hall Street* and other Supreme Court and federal precedent, there is no ground for this Court's review.

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[2] Presumably, that is why the Ninth Circuit denied Petitioner's Petition for Rehearing and Rehearing *En Banc*.

REASONS FOR DENYING THE PETITION

I. THIS CASE DOES NOT MERIT REVIEW BECAUSE THIS COURT'S RECENT DECISION IN *HALL STREET ASSOCIATES, LLC. v. MATTEL, INC.* ACTUALLY AGREED WITH THE NINTH CIRCUIT'S STATEMENT OF THE LAW, AND THE NINTH CIRCUIT'S DECISION IN THE CASE HEREIN IS CONSISTENT BOTH WITH ITS OWN AND WITH THIS COURT'S STATED RULE OF LAW.

Contrary to Petitioners' contention, the Ninth Circuit's decision herein does not conflict with this Court's decision in *Hall Street Assoc., LLC v. Matter, Inc.*, 552 U.S. ___, No. 06-989, slip op. 1-15 (March 25, 2008).[3] Rather, the Ninth Circuit is in accord with this Court's decision in *Hall Street*, which is why this Court actually agreed with Ninth Circuit decision that was being reviewed in *Hall Street* and upheld it.

Specifically, the question in *Hall Street* was "whether statutory grounds for prompt vacatur and modification may be supplemented by contract." (*Hall Street*, p.1) In reaching a decision on this issue, this Court addressed the split in authorities across the nation wherein some circuits regard the statutory grounds set forth in the FAA as exclusive grounds for vacatur of an arbitrator's award whereas others believe it is open to expansion by the parties' agreement. (*Hall Street*, p. 6) This Court concluded in *Hall Street* that

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[3] Page references herein to the *Hall Street* opinion are to the slip op.

the statutory grounds are exclusive and cannot be expanded by contract. (*Hall Street*, p. 1) This Court also found, however, that the Ninth Circuit is one of the circuits that actually complied with this standard. Specifically, this Court repeatedly and expressly "agreed" with the Ninth Circuit on the subject and concluded that the Ninth Circuit was applying the correct standard of review under the FAA. (*Hall Street*, pp. 4, 6 fn. 5, and 15.)

It should be noted that Petitioners never asserted in either their Appellee Brief nor in their Petition for Rehearing, below, that the Ninth Circuit failed to apply the appropriate ground for vacatur of arbitration awards under the FAA. Petitioners also never claimed that the "manifest disregard of the law standard" invoked by Respondents and applied by the Ninth Circuit was outside the permissible parameters of the FAA. Indeed, Petitioners never discussed Sections 10 and 11 of the FAA whatsoever. Rather, in response to the Ninth Circuit's ruling herein, Petitioners devoted pages of their Petition for Rehearing to discussing how "manifest disregard of the law" is essentially the law of the land throughout the circuits. [Resp. App. 7a-13a] It is disingenuous for Petitioners to now assert the opposite.

Moreover, contrary to Petitioners' arguments, *Hall Street* did not create a new rule for the Ninth Circuit, but rather affirmed the rule that the Ninth Circuit had been applying. Specifically, when the Ninth Circuit in this case vacated a portion of an arbitrator's decision because it was in "manifest disregard of the law", it was operating within the parameters set forth in *Hall Street*

and earlier Supreme Court decisions. Neither *Hall Street*, nor any other Supreme Court decision, states that the long established "manifest disregard of the law" standard is outside the scope of the FAA or that it is no longer valid.[4]

Indeed, as it has been established and historically reaffirmed by this Court, "manifest disregard of the law" has been an accepted standard for vacatur of an arbitrator's ruling under the FAA. (*Hall Street*, p. 8) (See, *Wilko v. Swan*, 346 U.S. 427 (1953)). The *Wilko* language was then accepted and cited by *First Options of Chicago, Inc. v. Kaplan*, 514 U.S. 938, 942 (1995) (stating that an arbitration award could be overturned if it was procured by corruption, fraud, or undue means, if the arbitrator exceeded his powers, and if the arbitrator's decision was "manifest disregard" of the law) (cite omitted).

This standard has been interpreted as a collective referral to the enumerated grounds set forth in Section 10 of the FAA. (*Hall Street*, p. 9) (See, e.g., *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 656 (1985) (Stevens, J., dissenting)). Indeed, even the court in *Luong* acknowledge that "manifest disregard of the law" is not in the words of the FAA

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[4] Petitioners' citation to *Luong v. Circuit City Stores, Inc.*, 368 F. 3d 1109 (9th Cir. 2004), to the contrary is a decontextualized and incomplete reference that is no more than a red herring here. [Petition, p. 8] The Ninth Circuit there did ***not*** say that the "manifest disregard of the law" standard fell outside the parameters of the FAA and specifically cited precedent as suggesting that **the "manifest disregard of the law" standard "really defines" Section 10 of the FAA**. (See discussion herein)

statute but still arises from it. See, *Luong*, 368 F. 3d at 1112 (citing *Todd Shipyards Corp. v. Cunard Line, Ltd.*, 943 F.2d 1056, 1059-60 (9th Cir. 1991) for the proposition that the "manifest disregard for law" standard "really defines" Section 10 of the FAA). This interpretation is consistent with the statutory construction of the FAA. In *Hall Street*, this Court expressly allowed for the assumption that Sections 10 and 11 of the FAA "could be supplemented to some extent". (*Hall Street*, p. 9) It follows logically that both the phrase "any other misbehavior [of the arbitrator] by which the rights of any party have been prejudiced" under § 10(a)(3) and "the arbitrators so imperfectly executed [their powers]" under § 10(a)(4) are broad enough to encompass a situation where arbitrators refuse to follow settled law and are therefore in manifest disregard of it. That is precisely what occurred in the case below and that is the reason that the Ninth Circuit vacated the offending portion of the arbitration award.

In sum, at no time did this Court in *Hall Street* conclude that the "manifest disregard of the law" ground for reversal of an arbitrator's ruling falls outside the enumerated penumbra in the FAA. The Ninth Circuit's decision herein that the arbitration award should be reversed because of the arbitrator's manifest disregard of the law does not conflict with this Court's recent decision in *Hall Street*.

There is no ground for Supreme Court review.

II. THIS CASE DOES NOT MERIT REVIEW BECAUSE THE NINTH CIRCUIT'S DECISION BELOW APPLIED THE WELL ESTABLISHED RULE THAT AN ARBITRATOR'S DECISION MAY BE REVERSED DUE TO THE ARBITRATOR'S MANIFEST DISREGARD OF THE LAW.

Petitioners' other asserted basis for granting certiorari review here is that the decision of the Ninth Circuit below allegedly conflicts with decisions of this Court and every other circuit applying the FAA by reversing an arbitrator's ruling for "mere errors of law." [Petition p. 9] This completely misrepresents the Ninth Circuit's decisions below both legally and factually.

The Petition is fundamentally incorrect. The Ninth Circuit below did *not* reverse the arbitrator's ruling because it was "in good faith" but "erroneous." [Petition p. 9] The Ninth Circuit also did *not* reverse the arbitrator's ruling because it just believed that he was "wrong". [Petition p. 14] The Ninth Circuit below reversed the arbitrator's ruling because it was in "manifest disregard of the law." [App. 27a] This is a historically established basis for reversing an arbitral ruling and it is consistent with the grounds set forth in the FAA. Petitioners have repeatedly conceded this.

Petitioners conceded in their Appellee Brief in the court below that "An arbitration award will be set aside only if it was made in 'manifest disregard of the law." (cite omitted) [Resp. App. 3a] Similarly, in their Petition for Rehearing and Rehearing En Banc, Petitioners again conceded that "manifest disregard of the law" is a valid

basis for overturning an arbitrator's decision. [Resp. App. 7a-13a] Even in the Petition herein, Petitioners cite countless opinions of practically every circuit court in the nation in support of this. [Petition pp. 12-14]

The real basis for Petitioner's seeking a writ of certiorari here is that they are unhappy with the resulting conclusion the Ninth Circuit reached when it applied the "manifest disregard of the law" standard, asserting that the Ninth Circuit "dramatically alters this 'manifest disregard' standard for review of an arbitration award." [Petition p. 7]. Merely disagreeing with the Ninth Circuit's ultimate ruling while acknowledging that it applied a properly stated rule of law does not constitute a compelling reason for justifying Supreme Court review of that ruling.

More importantly, the Ninth Circuit did not alter or misapply the "manifest disregard of law" standard below. Specifically, the Court's opinion below quotes verbatim the Ninth Circuit precedent for applying a "manifest disregard of the law" analysis to an arbitration award, stating that "[i]t must be clear from the record that the arbitrator [] recognized the applicable law and then ignored it." [App. 21a, citing *Mich. Mut. Ins. Co. v. Unigard Sec. Ins. Co.*, 44 F.3d 826, 832 (9th Cir. 1995) (bracketed text omissions in original)]. The Court below then proceeded to apply that standard accurately:

> Keeping in mind these settled principles of California law . . . we proceed to evaluate whether the arbitrator's decision was in manifest disregard of the law. [App. 25a]

* * *

> The arbitrator's award, while aware of *Dayton Time Lock*, interpreted it in a way to render it inapplicable to this case. [App. 26a]

* * *

> The arbitrator's ruling . . . ignores [California Business and Professions Code] CBPC § 16600 and thus is in manifest disregard of the law. [App. 27a]

Contrary to Petitioners' assertion that the Panel found that the arbitrator engaged in good faith but erroneous application of state law [Petition p. 9], the Ninth Circuit expressly found that the arbitrator's ruling "**ignores**" state law and, despite being aware of it, rendered it inapplicable and therefore ignored it in this case. [App. 26a and 27a] Hence, the Ninth Circuit applied the correct standard and applied it cogently and properly. Contrary to Petitioners' accusation, **the Ninth Circuit correctly applied the standard and acted consistently and in accordance with established Ninth Circuit precedent.**

Furthermore, the Petition is also incorrect in its baseless assertion that the Ninth Circuit's opinion conflicts with "every other circuit". [Petition p. 9] A review of the various circuits interpreting the issue, even if limited to the cases selected for citation in their Petition, demonstrates that the circuits themselves employ judicial flexibility in applying the "manifest disregard of the law" standard. But they all apply it.

In fact, far from Petitioner's contention, the circuits do not say that so long as an arbitrator evidenced a "good faith effort" to apply the law then his decision is not reversible. On the contrary, the cases Petitioners cite from the First, Third, Sixth, Tenth and Eleventh Circuits all echo the Ninth Circuit's explication of the "manifest disregard of the law" standard.

Indeed, most recently, the Second Circuit weighed in on the analysis with *Porzig v. Dresdner*, 497 F.3d 133 (2nd Cir. 2007), a decision Petitioners fail to cite to the Court. The Second Circuit Court there first articulated that the standard for reversal requires both that the arbitrators knew of a governing legal principle yet refused to apply it or ignored it altogether and that the law ignored by the arbitrators was well-defined, explicit and clearly applicable to the case. Based thereon, the Second Circuit overturned an arbitration panel's award of attorney's fees in favor of the Appellant based on a finding that the arbitrators demonstrated "manifest disregard of the law" because they inexplicably applied a contingency-fee agreement analysis to their calculation of the amount of attorney's fees rather than the loadstar method required by Second Circuit precedent. This analysis and conclusion is completely in line with the Ninth Circuit's decision herein.[5] It is, in fact, consistent with the majority of the circuits in the nation.

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[5] The Second Circuit's decision and application of the "manifest disregard of the law" standard particularly noteworthy not only because of its timeliness but also because New York statute is the basis for the FAA itself. *Hall Street*, p.12 fn.7.

The Fourth Circuit (stating that a party must prove that an arbitrator found a law applicable to the case but chose to ignore it[6]) and the Seventh Circuit (stating that the "manifest disregard" standard is only met when the arbitrator orders the parties to violate the law[7]) are themselves distinct from the majority of the circuits in that they interpret the "manifest disregard of the law" standard more acutely than the rest. **However, this is far from a split in the circuits or a failure of a circuit court to follow this Court's precedent.**

Petitioners try desperately to convince this Court that the Ninth Circuit's decision below is inconsistent with statutory, Supreme Court or existing Ninth Circuit authority. It is not. It is consistent both in its invocation of what is the applicable authority as well as in its analytical application of that authority within the context of this case. Accordingly, the Petition for writ of certiorari should be denied.

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[6] *Remmy v. PaineWebber, Inc.*, 32 F.3d 143, 149 (4th Cir. 1994).

[7] *Butler Mfg. Co. v. United Steelworkers of Am.*, 336 F.3d 629 (7th Cir. 2003).

CONCLUSION

Petitioners are simply, and predictably, attempting to get "another bite at the apple", and unfortunately using any means necessary (including misstating both the law and the Ninth Circuit's ruling). However, the Ninth Circuit here neither strayed from its own precedent nor from this Court's precedent. Rather, the Ninth Circuit reasonably and properly applied a well-established standard to reverse a portion of an arbitrator's ruling.

For the reasons set forth herein, the Petition for Writ of Certiorari should be denied.

Respectfully submitted,

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APPENDIX

APPENDIX A — EXCERPT OF BRIEF OF APPELLEES OF THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT DATED DECEMBER 19, 2005

Appendix A

Docket Nos. 05-55739(L), 05-56100

UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

COMEDY CLUB, INC. and AL COPELAND INVESTMENTS, INC.,

Appellants,

vs.

IMPROV WEST ASSOCIATES and CALIFORNIA COMEDY, INC.,

Appellees.

Appeal from the United States District Court for the Central District of California,
District Court No. CV 03-8134 WMB
Hon. Wm. Matthew Byrne, Jr.

BRIEF OF APPELLEES

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Appendix A

* * *

V. STANDARD OF REVIEW

A district court's confirmation of an arbitration award is reviewed *de novo*. *See Woods v. Saturn Distrib. Corp.*, 78 F.3d 424, 427 (9th Cir. 1996). Absent a showing to the contrary, the arbitrator is presumed to have relied on permissible grounds in making his or her decision and to have made an appropriate award. *See A.G. Edwards & Sons, Inc. v. McCollough*, 967 F.2d 1401, 1403 (9th Cir. 1992). An arbitration award will be set aside only if it was made in "manifest disregard of the law." *Michigan Mut. Ins. Co. v. Unigard Sec. Ins. Co.*, 44 F.3d 826, 832 (9th Cir. 1995). This stringent standard of review requires confirmation of an arbitration award "even in the face of 'erroneous . . . misinterpretations of law.'" *Todd Shipyards Corp. v. Cunard Line, Ltd.*, 943 F.2d 1056, 1060 (9th Cir. 1991). To vacate an arbitration award on the ground of manifest disregard of the law, it must be clear from the record that the arbitrator recognized the applicable law but chose to ignore it. *See Michigan Mut. Ins. Co.*, 44 F.3d at 832.

* * * *

APPENDIX B — EXCERPT OF PETITION FOR REHEARING AND REHEARING EN BANC OF THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT FILED SEPTEMBER 20, 2007

Appendix B

Docket Nos. 05-55739(L), 05-56100
Opinion Filed September 7, 2007
Before: Jerome Farris and
Ronald M. Gould, Circuit Judges,
and Kevin Thomas Duffy, District Judge

UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

COMEDY CLUB, INC. and AL COPELAND INVESTMENTS, INC.,

Appellants,

vs.

IMPROV WEST ASSOCIATES and CALIFORNIA COMEDY, INC.,

Appellees.

Appeal from the United States District Court for the Central District of California,
District Court No. CV 03-8134 WMB
Hon. Wm. Matthew Byrne, Jr.

PETITION FOR REHEARING AND REHEARING *EN BANC*

Appendix B

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Appendix B

ARGUMENT

A. The Panel's Decision Creates Serious Conflicts Of Authority Regarding The Standard For Review Of An Arbitration Decision

The Panel's ruling that the arbitrator's reasoned analysis of CBPC § 16600 constituted "manifest disregard of the law" conflicts with clear Ninth Circuit authority. As this Court (Kozinski, Fernandez, Rymer) recognized in *Luong v. Circuit City Stores, Inc.*, 368 F.3d 1109 (9th Cir. 2004), "manifest disregard of the law" has a well-defined meaning that does not reach errors of law, or even clear errors of law, by the arbitrator. *Luong* concerned an appellant's argument that the arbitrator had manifestly disregarded a controlling case, *Toyota Motor Mfg., Inc. v. Williams*, 534 U.S. 184, 122 S.Ct. 681, 151 L.Ed.2d 615 (2002), in rendering his award. This Court easily rejected the appellant's argument:

> . . . "[M]anifest disregard of the law" has a well-defined meaning that Luong's petition cannot possibly meet. "Manifest disregard of the law means something more than just an error in the law or a failure on the part of the arbitrators to understand or apply the law." *Mich. Mut. Ins. Co. v. Unigard Sec. Ins.* Co., 44 F.3d 826, 832 (9th Cir. 1995) (internal quotation marks omitted). "It must be clear from the record that the arbitrators recognized the applicable law and then ignored it." *Id.*

Appendix B

> Luong's complaint is that the arbitrator extended the ruling of *Toyota*, and thus disregarded it. However, without expressing a view one way or the other on whether the arbitrator got *Toyota* right, it is clear that the arbitrator did not *ignore* it. His written decision is part of the petition. Virtually every line of the opinion and award discussed *Toyota* and how it plays out on the facts in Luong's case. That cannot amount to "manifest disregard of federal law."

Luong, 368 F.3d at 1112.

The Panel's decision dramatically alters this "manifest disregard" standard for review of an arbitration award. The circumstances of this case are identical to those in *Luong*. CCI complains that the arbitrator misapplied CBPC § 16600 and thus disregarded it. However, it is clear that the arbitrator did not *ignore* CBPC § 16600. His written orders devote pages to a discussion of CBPC § 16600 and how it applies to the facts of this case. Under *Luong*, that simply cannot amount to "manifest disregard of the law."

The arbitrator similarly cannot be said to have disregarded *Dayton Time Lock Serv., Inc. v. Silent Watchman Corp.*, 52 Cal. App. 3d 1 (1975), a case that CCI did not even cite in the appeal but that became the lynchpin of the Panel's decision. The arbitrator did not ignore *Dayton Time Lock*, nor did he recognize that *Dayton Time Lock* controls the present dispute yet

refuse to apply it. Instead, the arbitrator considered the case and offered a reasoned explanation of why it is inapposite. SER 179. The Panel disagreed with the arbitrator's reading of *Dayton Time Lock* and found that "[t]he grounds given by the arbitrator for disregarding *Dayton Time Lock* are fundamentally incorrect." Opinion at 11849. However, the Panel's belief that the arbitrator was wrong, or even clearly wrong, is simply not relevant. The arbitrator's good faith determination that *Dayton Time Lock* is not applicable to the facts of this dispute, even if mistaken, cannot constitute "manifest disregard." At most, it reflects a misreading or misunderstanding of the case—*i.e.*, an error of law—that is not a valid basis for overturning the arbitrator's decision.[1]

The Panel's decision conflicts with the well-defined meaning of "manifest disregard" not only in the Ninth Circuit, but also under the controlling cases in *every other circuit.* In every circuit, the focus is not on

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1. *See A.G. Edwards & Sons, Inc. v. McCollough*, 967 F.2d 1401, 1403 (9th Cir. 1992) ("The courts should not reverse even in the face of erroneous interpretations of the law."); *American Postal Workers Union AFL-CIO v. U.S. Postal Serv.*, 682 F.2d 1280, 1285 (9th Cir. 1982) ("An arbitrator's award will not be vacated because of erroneous findings of fact or misinterpretations of law."); *see also Kyocera Corp. v. Prudential-Bache Trade Servs., Inc.*, 341 F.3d 987, 1003 (9th Cir. 2003) (en banc) ("[t]he risk that arbitrators may construe the governing law imperfectly in the course of delivering a decision that attempts in good faith to interpret the relevant law . . . is a risk that every party to arbitration assumes").

whether the arbitrator got the law right or wrong, but instead on whether he or she made a good faith effort to correctly apply the law. In *Lincoln Nat'l Life Ins. Co. v. Payne*, 374 F.3d 672 (8th Cir. 2004), the Eighth Circuit clearly distinguished between a good faith error of law, which is not a basis for overturning an arbitration award, and deliberate defiance of the law, which is: "Manifest disregard requires something more than a mere error of law. If an arbitrator, for example, stated the law, acknowledged that he was rendering a decision contrary to law, and said that he was doing so because he thought the law unfair, that would be an instance of 'manifest disregard.' . . . To require anything less would threaten to subvert the arbitral process." *Id.* at 674. Every other circuit has similarly determined that an arbitrator's good faith effort to correctly apply the law precludes a finding of "manifest disregard."[2]

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2. *E.g., First Circuit: Advest, Inc. v. McCarthy*, 914 F.2d 6, 10 (1st Cir. 1990) ("'[D]isregard' implies that the arbitrators appreciated the existence of a governing legal rule but willfully decided not to apply it."); *Second Circuit: Wallace v. Buttar*, 378 F.3d 182, 190 (2d Cir. 2004) ("A federal court cannot vacate an arbitral award merely because it is convinced that the arbitration panel made the wrong call on the law." ; *Third Circuit: Local 863 Int'l Bhd. of Teamsters v. Jersey Coast Egg Producers, Inc.*, 773 F.2d 530, 533 (3d Cir. 1985) ("An award may be set aside only in limited circumstances, for example, where the arbitrator's decision evidences manifest disregard for the law rather than an erroneous interpretation of the law."); *Fourth Circuit: Remmy v. PaineWebber, Inc.*, 32 F.3d 143, 149 (4th Cir. 1994) ("[A] court's belief that an arbitrator misapplied the law will not justify vacation of an arbitral award. Rather, appellant

(Cont'd)

Appendix B

(Cont'd)
is required to show that the arbitrators were aware of the law, understood it correctly, found it applicable to the case before them, and yet chose to ignore it in propounding their decision."); *Fifth Circuit: Brabham v. A.G. Edwards & Sons Inc.*, 376 F.3d 377, 381 (5th Cir. 2004) ("Manifest disregard means more than error or misunderstanding with respect to the law.") (internal quotation marks omitted); *Sixth Circuit: Merrill Lynch, Pierce, Fenner & Smith v. Jaros*, 70 F.3d 418, 421 (6th Cir. 1995) ("This court has emphasized that manifest disregard of the law is a very narrow standard of review. A mere error in interpretation or application of the law is insufficient.") (internal citation omitted ; *Seventh Circuit: Butler Mfg. Co. v. United Steelworkers of Am.*, 336 F.3d 629, 636 (7th Cir. 2003) ("[A]n arbitral decision is in manifest disregard of the law only when the arbitrator's award actually orders the parties to violate the law. That the arbitrator in this case may have misunderstood the [governing statute] is simply not relevant.") (internal citation omitted); *Eighth Circuit: Stroh Container Co. v. Delphi Indus., Inc.*, 783 F.2d 743, 750 (8th Cir. 1986) (manifest disregard "may be found when arbitrators understand and correctly state the law, but proceed to disregard the same."); *Tenth Circuit: Bowen v. Amoco Pipeline Co.*, 254 F.3d 925, 932 (10th Cir. 2001) ("Requiring more than error or misunderstanding of the law, a finding of manifest disregard means the record will show the arbitrators knew the law and explicitly disregarded it.") (internal citation omitted); *Eleventh Circuit: Aldred v. Avis Rent-A-Car*, 2007 WL 2110720, at *2 (11th Cir. July 24, 2007) ("An arbitrator manifestly disregards the law if he was conscious of the law and deliberately ignored it; merely misinterpreting, misstating, or misapplying the law does not suffice."); *District of Columbia Circuit: Kanuth v. Prescott, Ball & Turben, Inc.*, 949 F.2d 1175, 1182 (D.C. Cir. 1991) ("'Manifest disregard" may be found for example, if the panel understood and correctly stated the law but then proceeded to ignore it.").

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Far from deliberately defying CBPC § 16600, the arbitrator's orders reflect a good faith effort to correctly apply the statute in the context of an in-term covenant against competition. Indeed, as the District Court acknowledged, the arbitrator's application of CBPC § 16600 is perfectly *consistent* with the decisions cited by the arbitrator affirming the validity of in-term covenants under CBPC § 16600, including decisions of the California Court of Appeal (*Fowler*), the Eastern District of North Carolina (*Keating*), the Northern District of Illinois (*Great Frame Up*), and even this Court (*Shaklee*).[3] That cannot be "manifest disregard of the law."

In sum, the Panel's finding that the arbitrator's good faith but, in the Panel's view, erroneous application of CBPC § 16600 constituted "manifest disregard of the law" flies in the face of the uniform precedent of this

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3. Although *Shaklee U.S. Inc. v. Giddens*, 934 F.2d 324 (9th Cir. 1991), is an unpublished decision, and therefore is not binding precedent, the decision has been cited as persuasive authority by the Northern District of Illinois, the Eastern District of North Carolina, and the District of Utah and was considered by the arbitrator in this case. *Great Frame Up Sys., Inc. v. Jazayeri Enters., Inc.*, 789 F. Supp. 253, 255-56 (N.D. Ill. 1992); *Keating v. Baskin-Robbins USA Co.*, 2001 WL 407107, at *13 (E.D. N.C. Mar. 27, 2001); *SCO Group, Inc. v. Novell, Inc.*, 2007 WL 2327587, at *43 (D. Utah Aug. 10, 2007). The fact that a three-judge panel of this Court determined that *in-term* covenants against competition do not violate CBPC § 16600, even if not precedent, must preclude a finding that the same ruling by the arbitrator constitutes "manifest disregard of the law."

and every other circuit. The Panel's decision invites broad judicial review of arbitral decisions and, if permitted to stand, "could well jeopardize the very benefits of arbitration, rendering informal arbitration merely a prelude to a more cumbersome and time-consuming judicial review process." *Kyocera*, 341 F.3d at 998.

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FILED
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OFFICE OF THE CLERK
SUPREME COURT U.S.

No. 07-1334

IN THE
Supreme Court of the United States

IMPROV WEST ASSOCIATES and
CALIFORNIA COMEDY, INC.,

Petitioners,

v.

COMEDY CLUB, INC. and
AL COPELAND INVESTMENTS,

Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

REPLY AND SUPPLEMENTAL BRIEF OF PETITIONERS

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CORPORATE DISCLOSURE STATEMENT

The Petitioners, Improv West Associates and California Comedy, Inc., have no parent corporations, and no publicly held company owns 10% or more of their stock.

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REPLY AND SUPPLEMENTAL BRIEF FOR PETITIONERS

The Ninth Circuit has vacated an arbitrator's reasoned and good faith award for "manifest disregard of the law." This is not a statutory basis for vacatur under the Federal Arbitration Act ("FAA"), and the decision should be vacated and the case remanded for further consideration in light of this Court's decision in *Hall Street Assoc., L.L.C. v. Mattel, Inc.*, 552 U.S. ___, 128 S. Ct. 1396, No. 06-989, slip op. 1-15 (March 25, 2008).

Subsequent to the Petitioners' filing of their petition for a writ of certiorari, a circuit split has arisen regarding whether "manifest disregard" is a valid ground for vacatur under the FAA after this Court's decision in *Hall Street*. The First Circuit has ruled that, after *Hall Street*, manifest disregard of the law is not a valid ground for vacating or modifying an arbitral award under the FAA. The Second and Fifth Circuits have held to the contrary, ruling that even after *Hall Street* those circuits will continue to recognize "manifest disregard" as a non-statutory basis for vacating an arbitration award. As an alternative to vacating the Ninth Circuit's decision and remanding for further consideration in light of *Hall Street*, this Court should grant the petition for the purpose of resolving this circuit split regarding the non-statutory grounds, if any, upon which an arbitration award may be vacated.

Moreover, even if "manifest disregard" remains a valid ground for vacatur after *Hall Street*,

the Ninth Circuit's decision still conflicts with the law of every other circuit because the Ninth Circuit's decision allows a court to substitute its judgment for that of an arbitrator whenever the court disagrees with the arbitrator's understanding or application of the law. Although couched in terms of "manifest disregard," the Ninth Circuit's decision in fact sanctions ***de novo*** review of arbitration awards and should not be permitted to stand.

I. A Circuit Split Now Exists Regarding Whether "Manifest Disregard" Is A Valid Ground For Vacatur Under The FAA After This Court's Decision In *Hall Street.*

At the time Petitioners filed their petition, no circuit had ruled on whether "manifest disregard" remains a valid ground for vacating or modifying an arbitration award following this Court's decision in *Hall Street*. Subsequent to Petitioners' filing of their petition, a circuit split has arisen.

The First Circuit has ruled that, after *Hall Street*, "manifest disregard of the law is not a valid ground for vacating or modifying an arbitral award in cases brought under the Federal Arbitration Act." *Ramos-Santiago v. United Parcel Serv.*, 524 F.3d 120, 124 n.3 (1st Cir. 2008). In contrast, the Second and Fifth Circuits have continued to recognize "manifest disregard" as a non-statutory basis for vacating an arbitration award. *See Abondolo v. H. & M.S. Meat Corp.*, No. 07 Civ. 3870, 2008 WL 2047612, at *2 (2d Cir. May 12, 2008) ("[I]n this Circuit, courts will 'vacate an award only upon finding a violation of one of the four statutory bases

[enumerated in the Federal Arbitration Act ...], or, more rarely, if we find a panel has acted in manifest disregard of the law.'") (quoting *Porzig v. Dresdner, Kleinwort, Benson, N.A. LLC*, 497 F.3d 133, 139 (2d Cir. 2007)); *Moore v. Potter*, No. 07-20624, 2008 WL 1874566, at *4 (5th Cir. Apr. 28, 2008) ("This Court ... recognizes that an arbitration award may be vacated when an arbitrator manifestly disregards the law, which 'is an extremely narrow, judicially-created rule with limited applicability.'") (quoting *Prestige Ford v. Ford Dealer Computer Servs., Inc.*, 324 F.3d 391, 395-96 (5th Cir. 2003)).

Because the Ninth Circuit has not ruled on the continuing viability of manifest disregard as "***a non-statutory escape valve*** from an arbitral award," *Luong v. Circuit City Stores, Inc.*, 368 F.3d 1109, 1112 (9th Cir. 2004) (emphasis added), it is appropriate for this Court to vacate the Ninth Circuit's decision in the present case (which was decided before *Hall Street*) and to remand for further consideration in light of *Hall Street*. Alternatively, this Court should grant the petition to resolve the important circuit split that now exists as to the validity of "manifest disregard" as a ground for vacatur under the FAA.

II. Even If "Manifest Disregard" Remains A Valid Ground For Vacatur Under The FAA, The Ninth Circuit's Decision Conflicts With The Law Of Every Other Circuit And Sanctions *De Novo* Review Of Arbitration Awards.

To the extent that "manifest disregard" remains a valid ground for vacatur under the FAA,

the Ninth Circuit nonetheless departed from the law of every other circuit in holding that a court may vacate or modify an arbitrator's reasoned and good faith award simply because the court believes that the arbitrator has misunderstood or misapplied the law.

The portions of the Ninth Circuit's decision quoted in Respondents' opposition brief demonstrate the unprecedented nature of the decision. Respondents first quote the Ninth Circuit's holding that "[t]he arbitrator's award, while aware of [*Dayton Time Lock Service, Inc. v. Silent Watchman Corp.*, 52 Cal. App. 3d 1, 124 Cal. Rptr. 678 (1975)], interpreted it in a way to render it inapplicable to this case." Respondents' Opp'n at 9 (quoting App. 26a). The arbitrator did not, however, find that *Dayton Time Lock* required him to rule one way yet nevertheless proceed to rule the other way, which is the defining feature of "manifest disregard." *See* Petition at 12-14 and cases cited therein. Instead, the arbitrator read *Dayton Time Lock* to provide for a "rule of reason" analysis that is applicable only in the antitrust context. Specifically, the arbitrator analyzed *Dayton Time Lock* as follows:

> "[*Dayton Time Lock*], relied on by Respondent, is inapplicable. That case involved an attack on an exclusive dealing contract under the *antitrust laws*. The cases cited in the portion of the *Dayton* opinion relied on by Respondent involved validity of exclusive dealing contracts under the federal Sherman Act. The type of "rule of reason" analysis applied in

> antitrust cases-involving the determination whether a particular agreement unreasonably restricts competition generally in a defined geographic and product market-is not applicable to a determination of illegality under Section 16600. California's antitrust statute, the Cartwright Act, is separate and distinct from §16600 of the Business & Professions Code."

App. 90a-91a. Regardless of whether the Ninth Circuit agrees with the arbitrator's reading of *Dayton Time Lock*, the arbitrator certainly did not "ignore" *Dayton Time Lock* or render a ruling in willful defiance of that case. Instead, he analyzed and applied the case as he understood it. In concluding that this reasoned and good faith decision-making constitutes "manifest disregard" for which an arbitration award may be vacated, the Ninth Circuit has effectively sanctioned ***de novo*** review of arbitration awards.

The same is true with respect to the other passage of the Ninth Circuit's decision that is quoted in Respondents' opposition, in which the Ninth Circuit held that "[t]he arbitrator's ruling ... ignores CBPC § 16600 and thus is in manifest disregard of the law." Respondents' Opp'n at 9 (quoting App. 27a). Again, however, the Arbitrator neither ignored nor acted in defiance of section 16600 of the California Business and Professions Code. Instead, the arbitrator devoted a significant portion of his ruling to section 16600 and its application to the facts before him. To illustrate the point, it is

necessary to quote the arbitrator's ruling at some length:

> "Section 16600 of the California Business & Professions Code provides that "[e]xcept as provided in this chapter, every contract by which anyone is restrained from engaging in a lawful profession, trade or business of any kind is to that extent void." This provision is "an expression of public policy to ensure that every citizen shall retain the right to pursue any lawful employment and enterprise of their choice." *Metro Traffic Control, Inc. v. Shadow Traffic Network*, 22 Cal. App, 4th 853, 859 (1994). Although the language of Section 16600 is broad in scope, court decisions have upheld agreements limiting competition in a variety of contexts. For example, it has been, held that Section 16600 applies only to covenants preventing one from engaging in an entire business, trade or profession." *Campbell v. Board of Trustees of Stanford University*, 817 F. 2d 499, 502 (9th Cir. 1987). And covenants not to compete *during the term* of an employment agreement or distribution contract are regularly upheld. *Shaklee U.S., Inc. v. Giddens*, 1991 U.S. App. LEXIS 11617, *8-9 (9th Cir. 1991).
>
> ...
>
> "The authorities cited by the parties support the enforceability of in-

term covenants not to compete. Such covenants have been held enforceable during the terms of employments agreements, *Fowler v. Varian Assoc's Inc.*, 196 Cal. App. 3d 34, 44 (1987), supplier-distributor agreements, *Shaklee U.S., Inc. v. Giddens*, 1991 U.S. App. LEXIS 11617 (9th Cir. 1991), and franchise agreements. *Keating v. Baskin-Robbins, USA, Co.*, 2001 WL 407017 (E.D.N.C.) (applying California law) and *Great Frame-Up Systems, Inc. v. Jazayeri Enterprises, Inc.*, 789 F. Supp. 253 (E.D. Ill. 1992) (applying California law). Although the reasoning in these decisions is sparse, they do emphasize that in-term restrictions are only "partial" restraints on competition, because the restrained party (whether employee, distributor or franchisee) may continue to engage in the relevant business during the term of his or her agreement with the employer, supplier or franchisor. Respondent has not cited any decision invalidating in-term covenants not to compete under Section 16600.[6] The arbitrator finds, therefore, that paragraph

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"[6] Respondent has cited authorities striking down covenants not to compete in franchise or similar agreements *after* expiration of the contract term, but such decisions are inapplicable to paragraph 9.j as construed herein. *E.g., Scott v. Snelling and Snelling*, 732 F. Supp, 1034, 1042 (N.D. Cal. 1990); *Latona v. Aetna U.S. Healthcare, Inc.*, 82 F. Supp, 2d 1089, 1094 (CD, Cal. 1999)."

9.j of the Agreement is a valid and enforceable in-term covenant under California law.

"Alternatively, even if the paragraph 9.j covenant could be construed to extend beyond the contract term, it is enforceable up to the end of the contract term under California's "rule of severability," allowing enforcement of overbroad covenants up to their lawful temporal and geographical limits, *Swenson v. File.*, 3 Cal. 3d 389, 395 (1970); *Hill Medical Corp. v. Wycoff*, 86 Cal. App. 4th 895, 908 (2001). These decisions are more applicable to the present fact situation than *Kolani v. Gluska*, 64 Cal. App. 4th 402, 407-08 (1998), relied on by Respondent, which declined to convert an invalid covenant not to compete into valid trade secret protection clause. *Latona v. Aetna U.S. Healthcare, Inc.*, is also distinguishable. *Latona* held that an employer violated California public policy by firing an employee who refused to sign a covenant not to compete that violated Section 16600. The covenant prohibited all competition by the employee for six months after termination of employment, and thus clearly violated Section 16600. The Court held that the employer could not excuse its conduct by asking the Court to "reform" the contract to make it valid, either by excising the post-employment

> restraint or by converting it into a trade secret protection clause. The Court noted the *in terrorem* of allowing employers who require employees to sign Invalid covenants to use the Courts to reform such agreements when challenged. Such fact situations arc far removed from the present case, where the covenant does not expressly extend beyond the contract term and the parties are equally sophisticated and alert to their legal rights."

App. 104a-109a. The arbitrator further analyzed section 16600 in ruling on the Respondents' motion for reconsideration:

> "This motion amplifies an argument made in Respondent's reply memorandum (pp. 17- 20), which the arbitrator considered in making his summary adjudication ruling. The present motion is not a motion for reconsideration in the usual sense – no new law or newly discovered facts are cited. However, arbitration procedures are more flexible than court litigation and the motion will be considered on the merits.
>
> "Decisions assessing covenants not to compete under California Business & Professions Code §16600 consider whether the contract imposes total or partial restraints. *Campbell v. Board of*

Trustees, 817 F. 2d 499 (9th Cir. 1987). However, unlike some other states, California does not apply a "reasonableness" test in assessing the validity of a contractual restriction under §16600. *Campbell*, *supra* at 502; *Commercial Packaging. Inc. v. TIPS Package Engineering. Inc.*, 126 F. 3d 1131, 1133 (9th Cir. 1997).

"As determined in the summary adjudication order, the covenant not to compete in paragraph 9j of the Trademark License Agreement is a partial restraint on Respondent's ability to engage in the comedy club business. Indeed, the Agreement provides a framework for Respondent to engage in the comedy club business during the term of the Agreement, but only as a licensee of Claimant.

"Respondent argues that the covenant not to compete in paragraph 9j of the Trademark License Agreement will unreasonably impact Respondent, because of the limited number of clubs Respondent currently operates, the uncertain financial status of these clubs and Respondents' loss of its right to license additional clubs under the Agreement. This type of "unreasonableness" argument is not available under California law. *Id.* Moreover, Respondent's loss of the right

> to license new IMPROV clubs results from its own breach of the Agreement by failing to meet the development schedule, and Respondent should not be allowed to use its own default to invalidate an otherwise valid partial restraint on competition."

App. 89a-91a.

As above, there can be no question that the arbitrator analyzed and applied section 16600 as he understood it. The Ninth Circuit's ruling that the arbitrator "ignored" and acted in "manifest disregard" of section 16600 cannot be reconciled with the arbitrator's extensive discussion and reasoned analysis of section 16600. In truth, the Ninth Circuit simply disagreed with the arbitrator's reading of section 16600 and vacated the award on that basis. This ***de novo*** review of the arbitrator's award conflicts with the extremely limited review of arbitration awards provided for in the FAA and the decisions of every other circuit and, if permitted to stand, will open the floodgates to plenary review of arbitration awards.

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For the foregoing reasons and those stated in the petition, the petition for a writ of certiorari should be granted.

Respectfully submitted,

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